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Primoris Services Corp. (PRIM)

Q3 2021 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day and thank you for standing by. Welcome to the Primoris Services Corporation Third Quarter Earnings Conference Call. At this time, all participants are in a listen-only mode. After the speakers' presentation, there will be a question-and-answer session. [Operator Instructions] Please be advised that today's conference is being recorded. [Operator Instructions]

I'd now like to hand the conference over to your speaker today, Ms. Brook Wootton, Vice President, Investor Relations. Please go ahead.

Brook Wootton

Vice President-Investor Relations, Primoris Services Corp.

Good morning and welcome to Primoris' third quarter earnings conference call. Joining me today are Tom McCormick, President and Chief Executive Officer; and Ken Dodgen, our Chief Financial Officer.

Before we begin, I would like to make everyone aware of certain language contained in our Safe Harbor statement. The company cautions that certain statements made during this call are forward-looking and are subject to various risks and uncertainties. Actual results may differ materially from our projections and expectations. These risks and uncertainties are discussed in our reports filed with the SEC. Our forward-looking statements represent our outlook only as of today. We disclaim any obligation to update these statements except as may be required by law.

In addition, during this conference call, we will make reference to certain non-GAAP financial measures. A reconciliation of these non-GAAP financial measures are available on the Investor Relations section of our website.

I would now like to turn the call over to Tom McCormick.

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

Thank you, Brook. Good morning and thank you for joining us today to discuss our third quarter results and our financial outlook for the remainder of 2021. Our results show the strength of our overall business model and the strategic value of the acquisitions we have made in recent years. These acquisitions position us in key markets as our economy moves toward a zero carbon future. This is especially evident in our growing backlog. All along, we've said that we have tremendous opportunities in prospective projects, but while we announced some contracts in the third quarter, the fourth quarter is shaping up to be even stronger. The \$130 million solar project we announced last week is a good sign of things to come in this market.

Reflecting our confidence in our Future prospects, on November 3, our board of directors authorized a share repurchase program for the repurchase of up to \$25 million of outstanding common stock. Under the share repurchase program, we can, depending on market conditions, share price and other factors, acquire shares of our common stock on the open market or in privately negotiated transactions. Our board will reexamine the program again at the end of December 2022 when it expires.

You will also note that in our earnings release that we added some non-GAAP calculations. We hope this will make it easier for investors to compare our results with those of our peers on an apples-to-apples basis.

Year-to-date, our revenue was \$2.6 billion. This was driven by our Utility Segment revenue, which was up 21%, and our Energy/Renewables Segment revenue, which was up 16% over the same period last year. Year-to-date, net income was \$86.2 million, up 18% compared to last year. Our nine-month EPS is \$1.63, which is a 9% increase as compared to the same period in 2020. That increase is especially significant when you consider that we have 4.5 million additional shares from our secondary offering in the first quarter. When you look at our full-year EPS from 2017 to 2020, the CAGR increased over 15%.

In addition, our strategic focus on master service agreements is continuing to show results with 53% of our current backlog made up of MSA-based work. This is another record level for us.

For the third quarter, we generated \$913.2 million of revenue. Our solid performance in the Utility and Energy/Renewables markets demonstrates that our investment in these areas over the past several years continues to provide solid returns. Our Pipeline Segment revenue decreased by close to 50% as compared to the prior year. However, in 2020, we substantially completed \$127 million pipeline project during the same period.

Now, let's look at the three segments in detail. Our Utility Segment had a strong third quarter performance. Revenue came in at \$454.7 million. That is a 10% increase compared to the same period last year. This increase was primarily due to the addition of Future Infrastructure, which represented approximately \$65.1 million of revenue for the quarter. We continue to make progress on the integration of Future Infrastructure. The integration activities are more than 85% complete, having completed 450 of the approximately 520 activities.

Even as revenue rose, some of our operations continued to experience delays associated with customer design, material shortages, and slower permitting processes. This is all part of the COVID hangover impact, which is a market-wide challenge that we've previously discussed. However, we are now starting to see work that was held back earlier in the year ramping up and we expect it to be released in the first quarter of 2022.

Major operations activities during the quarter included sending approximately 300 crew members to assist with the power restoration efforts in the states along the Gulf Coast that were heavily impacted by hurricanes Ida and Nicholas. Our Utilities group continues to enter new geographic markets. As an example, during the quarter, we signed an MSA for emergency storm services with a northeast electric utility provider. This provider serves approximately 1.4 million customers in 29 different counties. We are targeting this market for additional work and should start to gain momentum over the next six months.

Future Infrastructure expanded its customer base and presence with the execution of new contracts to install aerial and underground fiber optic cable across the State of Texas. Two specific contracts to note include a \$15 million two-year MSA with a two-year optional renewal and an additional \$16 million two-year MSA. Both of these master services agreements will provide communications services to historically underserved communities. This work began during the third quarter of 2021. It is clear that the acquisition of Future Infrastructure is already bringing us opportunities as demand for data bandwidth continue to grow and we expect billions of dollars – actually we expect tens of billions of dollars of further investment in 5G and fiber networks to be required in order to keep up with the demand. We will continue to create synergies between Future Infrastructure and our other business units that will help create growth for our overall business.

Now turning to our Energy/Renewables Segment. Revenue increased to \$351 million for the quarter. That is an 11% increase over the same period the prior year. The biggest contributor was renewable energy activity, which grew by \$67.9 million. Operationally, we continue to make progress on the LNG project in the Northeast and we expect this project to be completed in the first quarter of 2022. The project is currently in the final stages of pre-commissioning activities of its mechanical systems.

Turning to contract activity, I mentioned last quarter that we were in late-stage discussions regarding a thermal power project in Southwest. In late August, we secured this \$100 million, 200-megawatt project. We've already begun the engineering and procurement and have recently mobilized to the field. The project should be completed in the second quarter of the next year.

In addition, we have over \$800 million in prospective projects. Many of these projects are currently working under limited notice to proceed in anticipation of full contract award. Final contracts for these projects should be executed over the next quarter.

Two of the LNTPs we mentioned last quarter for initial engineering work and long lead procurement on utility-scale solar facilities were finalized in the third quarter. One was for 101 megawatt project located in Midwest, the second was for 185 megawatt project that is located in the Southwest. Initial construction on both projects will begin work in Q4 of this year and will extend into the second and third quarters of 2022.

In addition, we recently announced another solar project award with an estimated value of \$130 million. The award is for the engineering, procurement and construction of a utility-scale solar facility in the Southwest. Early construction is scheduled to begin in the first quarter of 2022. The completion of the project is expected in the fourth quarter of 2022.

Our level of expertise and quality execution on solar projects are creating repeat opportunities from our clients. We are currently working with a client on multiple solar projects and they have recently awarded us a fourth project. This client has indicated they would like to partner with Primoris for multiple project teams on several projects over the course of the next three years.

One of Primoris' strongest and least appreciated assets are our customer relationships. We have contracts with companies that we have been working with on a relatively continuous basis for 20 years and longer through multiple contract types and contract renewals. And now we are building that same level of customer relationships in the solar market.

And beyond solar, other renewable natural gas and gas to liquids projects that were deferred during the pandemic are now moving into frontend engineering. As an example, we are set to perform the frontend engineering on Yosemite Clean Energy's renewable biofuels project. The facility will use gasification technology to convert farm and forest wood waste to syngas and ultimately into carbon-negative green hydrogen and renewable natural gas. This project takes advantage of our extensive experience in syngas, hydrogen and renewable natural gas production.

In October, we announced seven energy renewables heavy civil project awards with a combined value of over \$115 million. These projects are located across the Southwest. The awards start dates begin as early as the fourth quarter of 2021 and end in a range from the back half of 2023 through mid-year 2024.

The \$225 billion renewables market continues to expand and we are positioned to grow with it. A recent US Department of Energy study notes that by 2035, solar energy has the potential to power 40% of the nation's electricity. This study also indicated that in order to accomplish this, annual solar capacity additions or installed will likely need to quadruple over the next decade. That means going from 15 gigawatts per year in 2020 to close to 60 gigawatts per year in 2030. The DOE report also highlights the need for new tools that increase grid flexibility. This includes storage [indiscernible] (10:54) as well as transmission expansion that will help move solar energy to all parts of the country. All this grid modernization fits perfectly within our capabilities and will drive our growth for years to come.

We will have over \$1 billion in backlog as we close the year for work associated with 2022 and 2023 solar projects. Even as we build our backlog of renewable energy projects, our more traditional heavy civil business continues to perform well. We've been notified of an award and are in the process of a contract execution on a Gulf Coast project that is scheduled to commence in Q1 of 2022 and extend into 2027. The Energy/Renewables Segment backlog will increase to approximately \$1.7 billion by the end of the year with the addition of this project.

Moving on to our Pipeline Services Segment, after an exceptional 2020, this year continues to play out more in line with its 2019 performance. Revenue came in at \$107.6 million for the quarter. While this is a decrease year-over-year, it is slightly ahead of our expectations for the quarter. One contributor was the higher productivity we achieved from the outset of a major pipeline project, in which we completed all the mechanical work during the quarter. In August, Hurricane Ida impacted most of our projects along the Gulf Coast, including this one. We are currently completing our punch list items and expect project completion and acceptance by the customer this quarter.

Another pipeline project in Nevada was completed on schedule and significantly under budget. This benefited this segment's Q3 results. Most of our other pipeline projects are on track. We have two large projects operating ahead of plan and on budget. We anticipate our West Coast project will resume in early Q4 or early to mid-Q1. This project recently experienced delays associated with approvals and permits.

As we expected, the increase in commodity pricing as well as some renewed understanding of the need for reliable, affordable, dispatchable energy across the world has increased the project development activities of our customers. The push towards carbon neutrality has led to additional opportunities for construction of renewable natural gas pipelines. We are seeing major carbon capture projects being released for bid, including one which is

tentatively budgeted for \$350 million to \$400 million just for the facilities work alone. This is a reminder that our expertise extends across all types of pipelines, whether it be transporting natural gas, crude oil, refined products, NGLs, carbon dioxide, or water.

Primoris Pipeline is working with Primoris Renewable Energy to utilize some of their pipeline resources and expertise in order to help PRE expand their budget capacity. This will help us leverage the project execution and management expertise that exists across all of Primoris business units.

Now, moving back to the big picture. Across the board, we are focused on working with our customers to address and alleviate supply chain issues. That means we are ordering materials ahead of our normal schedule. We're increasing our CapEx to order equipment now for delivery in 2023. We're also focused on being disciplined about the projects we undertake so that we stay true to our strategy and manage our risk profile. And as always, we are focused on the health and safety of our workers.

Across our businesses, we maintained a superior safety record. Through first nine months of the year, our total recordable incident rate 0.53, which is ahead of our corporate target of 0.60. As of the end of September, 16 of our 19 business units had zero lost time injuries and 5 of the 19 business units had zero recordable injuries year-to-date.

COVID-19 remains a health and safety priority. We continue to follow CDC guidelines as well as protocols established by our clients for their sites. We also continue to encourage our employees to get vaccinated. In regards to the vaccine and testing mandate for companies with more than 100 employees, we are watching this go through the various legal hurdles and are in the process of creating a plan to comply with whatever is ultimately required by OSHA.

We are designing a plan that addresses four elements. First of all, validation and/or documentation relating to which employees are vaccinated; and second, testing of unvaccinated employees to meet the requirements determined by OSHA; third, evaluating the impact this will have on our multiple labor agreements; and finally, evaluating the legal implications to our contracts and MSAs with our clients.

Before I hand off to Ken for a review of the numbers, I want to take a moment to look forward. As you can see, we are well-positioned to meet the needs of the changing energy infrastructure across North America as it transitions to a zero carbon future with more energy coming from renewable sources, grid modernization and greater reliance on broadband and 5G technology. Electrification is a huge piece of this to support the electric vehicle fleet as well as other technology additions to the power load. In line with this transformation, our revenue mix is shifting from almost exclusively conventional energy and civil infrastructure to a large and growing proportion of solar energy, electric grid transformation, and communications infrastructure.

We have spoken previously about the potential impact of the Infrastructure Bill Congress has been working on. None of that potential has been baked into our current projections. Now that it has passed in the House, whatever opportunities come to our business units from this bill will be pure upside for us. We have to see what actual projects materialize, but I can only see positive news in this legislation for Primoris.

We are in unprecedented times, not just because of the energy transition, but because so much of everything we do has been, is or will be impacted by the global COVID-19 pandemic. Nearly 21 months ago, after the virus first triggered, workplace and social shutdowns, none of us accurately predicted how the pandemic would be affecting workplaces, processes, and supply chains. Yet we do know that the short-term disruptions in some ways are

accelerating the urgency of some of the long-term trends, such as grid modernization and the expansion of broadband, even as the implementation has been slowed by the pandemic.

As we emerge from this pandemic, we at Primoris believe that the underlying demand for our services has not abated. We are here for the long game and intend to be a leader in contributing to the strength of our communities and our country as we build America's infrastructure in new and more sustainable ways.

And with that, I'll now turn it over to Ken.

Kenneth M. Dodgen

Chief Financial Officer & Executive Vice President, Primoris Services Corp.

Thank you, Tom, and good morning, everyone. Let me begin with our key operating metrics for the third quarter and then I'll discuss our balance sheet, cash flows, and backlog. I'll wrap up with our guidance before moving on to your questions.

Our third quarter revenue was \$913.2 million, a decrease of only \$29.5 million compared to the prior year. The decrease was primarily driven by \$106.8 million decrease in pipeline work as expected, offset by a \$41.4 million increase from the Utility Segment and a \$35.9 million increase from the Energy/Renewables Segment.

Despite the decline in revenue, gross profit for the third quarter was \$127.4 million, an increase of \$3.8 million. The increase in gross profit was primarily due to the acquisition of Future and good project closeouts for the Pipeline Segment. Gross margins increased to 14% for the third quarter compared to 13.1% for the prior year.

Now, let's look at each segment. Energy/Renewables revenue was up by \$35.9 million compared to the prior year on the continued strength of our renewables work, which increased by over \$50 million compared to the prior year. Gross profit was \$35.9 million, an increase of \$8.4 million or 30.7% compared to the prior year. This is primarily due to higher revenues and margins. Gross margins increased to 10.2% during the quarter compared to 8.7% in the prior year. This was mainly due to higher costs associated with the LNG plant project in the Northeast in 2020.

Despite the lower revenue in our Pipeline Segment, we generated gross profit of \$27.8 million, which was slightly below the \$28 million we made in the prior year. Gross margins came in at 25.8% for the quarter. This was primarily due to some favorable project closeouts during the quarter. While it's nice to finish strong on these projects, I expect fourth quarter pipeline margins to be back to our normal range of 9% to 13%.

Utility Segment revenue was up \$41.4 million in the quarter, with Future contributing \$65.1 million, offset by slightly lower revenue from our legacy operations. Many parts of our Utility Segment, including Future, faced headwinds from both project and material delays related to COVID-19. And our electric operations in Texas were impacted by the ERCOT moratorium for most of the quarter. These temporary issues resulted in lower revenue, idle equipment, and lower crew utilization. Despite these headwinds, we generated 14% gross margins during the quarter compared to 16.5% in the prior year.

I'll also remind you that last year's gross margins had the benefit of near record storm work that contributed an extra 1% of gross margin. Taking all of this together, gross profit was \$63.7 million for the quarter, down \$4.4 million from the prior year. Future contributed \$11.4 million of gross profit with gross margins of almost 18% this quarter.

SG&A expense in the third quarter was \$61.7 million, up from \$57 million in the prior year. The increase was due to \$6.5 million of incremental SG&A from the Future acquisition, which is less than what we originally expected for the quarter. As we continue to integrate Future, we expect our SG&A as a percent of revenue will continue to be in the mid-6% range for the full year 2021. And once we complete the integration, next year's SG&A should be back down in the low 6% range.

Interest expense in the third quarter was \$4.7 million. This is in line with the prior year. The consistency in interest expense was due to higher debt balances in the current year, driven by the Future acquisition, offset by lower average interest rate this year.

Our effective tax rate during the third quarter was approximately 27.5% compared to 29% for the prior year. We expect our full year effective tax rate to be approximately 27.5% as we are seeing more of our work coming from states with lower state income tax rates.

Net income was \$44.1 million for the quarter, slightly better than the \$44 million in the prior year. Diluted EPS was \$0.81 compared to \$0.90 in the prior year as a result of the dilution from our first quarter equity offering.

As Tom mentioned earlier on the call, we have implemented three new non-GAAP metrics to be more comparable to our peer group and to make our results more comparable from quarter-to-quarter and year-to-year. We have added adjusted net income, adjusted EPS, and adjusted EBITDA.

Let's start by discussing our adjusted EPS. These adjustments include non-cash stock-based compensation, transaction, integration and related costs, amortization of intangible assets, amortization of debt issuance costs, unrealized gain or loss on interest rate swap, and the cumulative income tax impacts of these adjustments. After making these adjustments, our adjusted EPS was \$0.89 per share for the third quarter compared to \$0.93 per share in the prior year. And year-to-date, our adjusted EPS is \$2.04 per share compared to \$1.69 in the prior year.

Adjusted EBITDA for Q3 was \$94.7 million, an increase of 8% compared to \$87.9 million for the same period in 2020. And year-to-date, adjusted EBITDA was \$230.8 million, a 25% increase compared to \$184.7 million in the prior year. The EBITDA adjustments include non-cash stock-based compensation and transaction and integration and related costs.

Now, let's move to operating cash flows. In the third quarter, operating cash flows were \$9.3 million and year-to-date they were \$14.9 million. The decrease in operating cash flows in 2021 was mainly due to lower deferred revenue this year as a result of the decline in pipeline work and the \$43 million deferral of FICA tax payments under the CARES Act in 2020.

In the third quarter, we invested \$39.4 million in CapEx, of which \$35.9 million was used for construction equipment. And year-to-date, we've invested \$102.1 million in CapEx with \$91.7 million invested in construction equipment. We have increased our spending on equipment this year in preparation for the growth we're expecting next year and beyond. We expect our remaining 2021 capital spending to be in the \$10 million to \$20 million range, with almost all of that spent on construction equipment.

We ended the quarter with \$199 million of cash. Borrowing capacity under our revolver was \$155.5 million, providing total available liquidity of \$354.5 million at quarter-end. Total debt was \$678.6 million and net debt was \$479.6 million.

Over the next 12 months, we expect to use our cash and operating cash flows to support the continued organic growth of our company, reduce debt, and to pursue acquisitions that complement our growth strategy. Total backlog at the end of the quarter was \$2.7 billion, down approximately \$131 million from the end of Q2 as we burn through some fixed pipeline backlog and saw the timing of certain new awards temporarily delayed into the fourth quarter. Our MSA backlog remained flat at \$1.5 billion at the end of the quarter, which is a record 53% of total backlog.

And concluding with our 2021 earnings guidance, as a result of the temporary headwinds we've experienced the past couple of quarters, we are adjusting our guidance range and expect earnings per fully diluted share to be in the \$2.10 to \$2.20 range and we are adding adjusted EPS guidance, a non-GAAP measure, which we expect to be between \$2.61 and \$2.71 per share.

With that, we can turn it over to your questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] First question comes from the line of Sean Eastman from KeyBanc Capital Markets. Your line is open.

Sean D. Eastman

Analyst, KeyBanc Capital Markets, Inc.

Q

Hi team. Thanks for taking my questions. Could you just maybe refresh us on what's happening under the hood in the Utilities business? The legacy revenues are down year-over-year. Maybe just understanding what's happening in T&D versus LDC. And FIH revenues I feel like have come in below expectations through this year. So, just a little more color on what the softness is on FIH specifically as well would be helpful.

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

A

Yeah. Sure, Sean. This is Tom McCormick. Yeah. The FIH is we've talked about it for the most – largest part of the year. The revenues are down. They're going to be down roughly \$70 million. I'll let Ken correct me if I misspeak for the year. And it's just been really slow start to their years. But I'll tell you their performance, especially towards the – as we approach the end of year exactly where we expected on the margins [indiscernible] (27:00) high double digits. There's really a good outlook for next year. I think next year is going to be an exceptional year for them. And when we start looking at their revenues and [indiscernible] (27:20) where we thought they would be or should have been. So, FIH I think is really going to be off to a good start at the beginning of next year. I think they're going to finish the year pretty strong.

Gas. Again, one thing you have to think about is we talked about COVID hangover with respect to gas and T&D, they got off to a little bit slow start. And in T&D, there's been a couple things that have hurt them. The weather events that we talked about in the first quarter and second quarter have slowed both of those businesses down with respect to any work in Texas. But the balance of it has been really just delays by either clients issuing work orders and they probably haven't been issuing work orders because either they don't have the materials, they haven't finished the engineering, or the COVID impacts. And a lot of that's very typical with what we've seen in the past when the economy slows down typically construction suffers the next year because clients will pause, which a lot of their clients did at the beginning of this year to wait and see what's going to happen with COVID and what's going to happen with the economy. And then they launch off into their year.

I expect our gas group – gas distribution group to have a good year next year. I think they're going to finish the year strong. A lot of that depends on the weather because some of their work up in the central part of the US and in the North is impacted by the weather. They're still working right now. Typically on an average year, they'll work through the end of November, but they'll start slowing down in December. In good years, they get to work all the way through the end of the year, and we'll just see how that works.

Transmission and distribution, there's been a little bit of pressure with respect to wage, battle for overhead crews. We've just seen some increases there so we've been in a lot of competition for the labor. But when you get down into substations and the distribution work they do, they're actually performing very well. And I think there was a slowdown in some of the projects, especially during the ERCOT work stoppage that happened this summer. And of course, they also lost two weeks in the first quarter, two weeks in the second quarter. But when you talk about the ERCOT moratorium this summer, they lost project work. So, that's really what's impacted them this year.

And on top of that, you consider the fact that last year we had a record year with respect to storm restoration work, and this year has been very minimal, at best. We don't bake a lot of that into our plans, but we do have some up in our plans, and it's actually below plan this year. We're not going to put much of it in our plan next year, and it'll just be an upside. But we're expecting a lot of project work next year. Some of our major clients in transmission and distribution, they're doubling, they're basically increasing their spend 50%, and we expect our budgets to go up with theirs. So I think 2022 is going to be a great year for them.

Sean D. Eastman

Analyst, KeyBanc Capital Markets, Inc.

Q

Okay. Helpful rundown there. And then moving over to the Pipe Segment, sounds like there's some green shoots on the traditional side and, of course, on the energy transition side. But as we think about the next 12 months, do you think revenues sort of settle here at this run rate in the third quarter or is there more downside on the top line? And at this level of revenue, what kind of margin profile should we be thinking about? I mean, the 9% to 13% target range is really wide, right? So, just kind of curious in that spectrum how we should think about the business at this kind of run rate.

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

A

Sure. So I'll hit on the workload of what we think the revenues are going to be and I'll let Ken hit on the margins. But I would expect their margins to be very similar to where they were this year. They're going to be somewhere in the \$450 million to \$500 million range.

Kenneth M. Dodgen

Chief Financial Officer & Executive Vice President, Primoris Services Corp.

A

Revenue.

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

A

Revenue. But when you start – and it's going to be probably that – I would expect it's going to be that way through the first half of next year. I think what happens with carbon capture is going to determine what happens at the backend of the year. We are seeing some work activity. We are bidding some projects. We are working with clients on some estimates for carbon capture projects. You heard me mention them in the earnings call of the one project that is roughly \$350 million to \$400 million just on facilities work alone. And if I'm not mistaken, I think that

pipeline work is close to 2,000 miles of pipeline and gathering and collection and transmission of that carbon dioxide somewhere. So, if that project goes or further projects like it goes, the back half of the year could be very good. But we're looking at \$450 million to \$500 million. That's where I would set expectations.

Kenneth M. Dodgen

Chief Financial Officer & Executive Vice President, Primoris Services Corp.

A

Yeah. And the margins, yeah, even though 9% to 13% is a little bit wide, that's just indicative of where we are in those jobs, right? And so, if we're early on in the job, we might be on the lower end of the range and the timing of certain jobs. But if we're toward the end and we're closing it out, we could be toward the upper end of the range. I think the sweet spot is going to be right in the middle. It's going to be kind of 10% to 12%.

Sean D. Eastman

Analyst, KeyBanc Capital Markets, Inc.

Q

Okay. Very helpful. And the CapEx guidance came down a lot. Does that impact your ability to grow in any of these segments next year? And I mean, more broadly, how should we think about CapEx on a go forward with Pipeline now representing a lower portion of the mix? Does that take down the capital intensity in the business?

Kenneth M. Dodgen

Chief Financial Officer & Executive Vice President, Primoris Services Corp.

A

Yeah. So I'll answer your second question first. No, because, there's still a pretty significant CapEx requirement for utility crews and even for some solar work as well. But with respect to CapEx, actually, while the guidance came down for Q4, for full year we're actually going to be above what we originally said. And that's because we had a pretty big spend for Q3. And as I mentioned in my comments, part of that reason for that big spend in Q3, and Tom touched on this as well, is getting ahead of the equipment needs for the growth we're expecting next year.

Sean D. Eastman

Analyst, KeyBanc Capital Markets, Inc.

Q

Okay.

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

A

I think we even said we're going to spend somewhere between \$10 million and \$20 million in the fourth quarter, maybe even a little bit more than that to make sure that we get out in front of these orders because their vehicle and equipment suppliers are saying if you don't get orders in now for 2023 or late 2022, you're not going to get your equipment. We're actually investing ahead to make sure we get what we need for growth.

Sean D. Eastman

Analyst, KeyBanc Capital Markets, Inc.

Q

Okay. I heard that wrong. Helpful clarification there. All right. Thanks a lot, guys. I'll turn it over there.

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

A

Thanks, Sean.

Kenneth M. Dodgen

Chief Financial Officer & Executive Vice President, Primoris Services Corp.

Thanks, Sean.

A

Operator: Next question comes from the line of Lee Jagoda from CJS Securities. Your line is open.

Q

Yes. Good morning .It's [ph] Pete Lukas (33:55) for Lee. You touched on a lot of this, but could you just mention again looking at the guidance, can you clarify which segments you're seeing the biggest headwinds from the delays and whether you expect for Q4 to be mostly a revenue headwind or margin weakness as a result looking specifically at Q4?

Kenneth M. Dodgen

Chief Financial Officer & Executive Vice President, Primoris Services Corp.

Looking at Q4, I think a lot of the headwinds we've had in the utility space are going to start to trail off a little bit. Pipeline is going to continue to be fairly steady state in Q4 and Energy/Renewables is going to be fairly steady state in Q4 as well, maybe down just slightly due to normal seasonality in Q4. And most of it is revenue headwinds that we're talking about right now.

A

Q

Helpful. Thanks. And just one more for me. Can you quantify the positive true-up you had in Q3 for the Pipeline Segment revenue and margin? And should we expect any additional true-ups in Q4 that are included in the guidance range?

Kenneth M. Dodgen

Chief Financial Officer & Executive Vice President, Primoris Services Corp.

Yeah. I mean, the margins for pipeline came in at 25.8% for the quarter, gross margins did. Our normal range is 9% to 13%. So I think you can back into anything above 13% will get you to your number. And then in Q4, no, Q4 is probably going to be fairly steady state with respect to Pipeline margins.

A

Q

Very helpful. Thank you.

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

Thanks, [ph] Pete (35:25).

A

Operator: Your next question comes from the line of Adam Thalhimier from Thompson Davis. Your line is open.

Adam Robert Thalhimier

Analyst, Thompson Davis & Co., Inc.

Q

Hey. Good morning, guys.

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

Hey. Good morning, Adam.

A

Adam Robert Thalhimer

Analyst, Thompson Davis & Co., Inc.

Can you comment on the Gulf Coast industrial award? That sounded interesting. Just curious what your scope is on that.

Q

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

Trying to think of what.

A

Kenneth M. Dodgen

Chief Financial Officer & Executive Vice President, Primoris Services Corp.

Gulf Coast industrial award.

A

Adam Robert Thalhimer

Analyst, Thompson Davis & Co., Inc.

I thought you said there was something in the energy segment that was going to take the year-end backlog.

Q

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

In energy, there's a power generation facility that's out on the West Coast, it's \$100 million that we were awarded. It's basically a simple power plant that we're designing and building. And there's another one that we're bidding or negotiating and it's behind that one. I know we referred to that.

A

Adam Robert Thalhimer

Analyst, Thompson Davis & Co., Inc.

I thought there was something in the energy segment that was going to take the backlog to \$1.7 billion?

Q

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

Okay. That's the heavy civil award for a project along the Gulf Coast and it's...

A

Adam Robert Thalhimer

Analyst, Thompson Davis & Co., Inc.

That was heavy. Sorry. I thought I heard that as an industrial.

Q

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

Heavy civil falls in our Energy/Renewables Segment. Remember, we resegmented at the beginning of the year.

A

Adam Robert Thalhimer

Analyst, Thompson Davis & Co., Inc.

Q

Okay. But then, I guess, what are you seeing in general Gulf Coast industrial then?

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

A

Seeing a lot of opportunities, a lot of them are related to renewables, either renewable gas, biofuels. We're seeing some pickup in just the industrial markets with the refiners coming out now with some plans and projects for 2022 and going into 2023. We mentioned a FEED study that we're doing on a renewable natural gas project. You're not seeing megaprojects which is good because we don't do megaprojects. We are subcontractors on those, but there seems to be a number of projects that are in that 150-down million dollar range. And we're seeing the market lighten a little bit. We had a lot of pressure on companies bidding those last year. We were in pretty good position on a number of them with some of our traditional clients.

Adam Robert Thalhimer

Analyst, Thompson Davis & Co., Inc.

Q

Got it. And then can you comment on the solar side, what you're seeing with panels?

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

A

It really depends on the type of panels the clients are utilizing and we're involved in those projects pretty early. As we've talked about in the past, it takes six to nine months, really, to develop a project from the initial bid or initial discussion of project budgets to entering into a full EPC contract award. So, the clients that are bidding projects are buying panels from suppliers that have longer leads. We're either getting them to buy those panels earlier or we're extending their schedules to show them what the impacts are. Most of the clients, we're guiding them, and they're buying the panels early to ensure that they have supply. We've had some projects that have seen some delays, but really it's only just small impacts [indiscernible] (38:35) maybe with a certain section of the facility's panels coming in later than expected.

Adam Robert Thalhimer

Analyst, Thompson Davis & Co., Inc.

Q

Okay. That's helpful. I'll turn it over. Thank you.

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

A

All right. Thank you.

Kenneth M. Dodgen

Chief Financial Officer & Executive Vice President, Primoris Services Corp.

A

Thanks, Adam.

Operator: Next question comes from the line of Jerry Revich from Goldman Sachs. Your line is open.

Jerry Revich

Analyst, Goldman Sachs & Co. LLC

Q

Yes. Hi. Good morning, everyone. Can we just talk about the solar? Been a nice sequential acceleration in revenue 2Q to 3Q. Can you just talk about what you're seeing in terms of was that projects ramping up or hitting the sweet spot from a revenue burn standpoint? And can you update us on where you stand on your ability to increase the crew count heading into year-end? Thanks.

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

A

Yeah. I mean, we're still working to add crews. We've been successful in adding a number of them that we need to support the work that we have under contract or on our schedules right now for the balance of this year and for into 2022. We'll continue to build crews and pursue work. But we're not going to take on any more work than we can manage and staff. But we're having some success there. Obviously, it gets a little bit tighter as you continue to build. But the opportunities are huge. I mean, I can't speak to the revenue that we burn on these projects, but under contract right now we have just under \$800 million under contract.

We have another \$1.1 billion that's under LNTF right now. So that'll enter into project execution sometime either later this year or in 2022. That will be executed in 2022 and 2023. And then we have another \$800 million of projects that we're sole sourced on right now. It doesn't mean they're going to move forward. They've got to get financial approval. But most of them, a number of them will move forward. So, the market is huge. It's a 225 billion plus dollar market. We're going to continue to push our clients and [indiscernible] (40:36) continue to push to replace power generation with fossil fuels with renewables. They're probably going to have to quadruple how many facilities we build from 15 gigawatts a year to 60 gigawatts a year, which will put pressure on us and everybody else to grow. So, this business you're going to see significant growth next year from this business from where it is, where it's going to finish this year, and we're going to continue to grow it.

Jerry Revich

Analyst, Goldman Sachs & Co. LLC

Q

And is it possible to just put a finer point on that? Can we grow the crew count by 30%? Can you just maybe just quantify how quickly you're able to [indiscernible] (41:18) staffing constraints?

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

A

I'd say in a year we can probably grow the crew count anywhere from 25% to 30% a year, which is about two, maybe a little bit more crews, full crews a year. The business – last year I think it'll grow close to 50% this year from last year. Next year, it'll probably be half of that. You're just not going to grow at the same rate every year because it gets more and more difficult to do that. Plus, we just don't want to get out of our skis too much. So, we're going to grow at a controlled rate.

Jerry Revich

Analyst, Goldman Sachs & Co. LLC

Q

Okay.

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

A

But the opportunity is there.

Jerry Revich

Analyst, Goldman Sachs & Co. LLC

Yeah. And then on the pipeline – sorry, please go ahead.

[indiscernible] (41:58)

Q

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

Okay. So, you did hear me mention that our Pipeline group now is actually providing some management personnel to PRE. They're working with PRE to help develop their people so that they can, in the interim, there is not pipeline work, they can build their management teams with pipeline management teams and build their capacity. So, there's an opportunity there, too. We're doing some cross-training to see what other businesses can provide services to our Renewables group. Also because, look, we built substations, we do underground electrical, we do transmission lines. So, wherever we can actually do work and complement what they're doing for their clients and add revenue to our backlog, we're looking at.

A

Jerry Revich

Analyst, Goldman Sachs & Co. LLC

Okay. And on the Pipeline group, you folks have delivered a steady job of [indiscernible] (42:53) closeout benefits over the past three quarters. Can you just talk about what's the schedule of project closeouts in terms of the [indiscernible] (43:01) expected to close in 4Q and 1Q and what's the magnitude of those closeouts? How does that compare versus the magnitude of projects that you folks finish up over the first three quarters? Just to help us get a sense whether we might get another upside surprise here.

Q

Brook Wootton

Vice President-Investor Relations, Primoris Services Corp.

Do you mind repeating the question? It cut out quite a bit.

A

Jerry Revich

Analyst, Goldman Sachs & Co. LLC

Sure, Brook. Can you hear me better now?

Q

Brook Wootton

Vice President-Investor Relations, Primoris Services Corp.

Yes.

A

Jerry Revich

Analyst, Goldman Sachs & Co. LLC

Okay. Perfect. I was saying, in Pipeline, you had three quarters now really outstanding project closeout benefits. So I'm wondering if you can talk about for the fourth quarter and the first quarter, what's the [indiscernible] (43:43) expect to close out and finish up. And how does that compare to the number of projects and the size of projects that you finished up over the first three quarters, just to help us get a sense for whether we could see another upside surprise potentially if things go well.

Q

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

A

Yeah. So, Jerry, I think quick answer is most of the project closeouts that you've seen over the course of the past two to three quarters are really wrapping up some of those big projects that we worked on that we had started last year, which part of what drove last year to be such a big year and then the remnants coming into this year.

In terms of Q4 and Q1 and I touched on this a little bit earlier. With respect to Q4, I don't expect any big project closeouts. And really with respect to Q1, I don't either. We don't have any big larger project we're working on. A lot of what we're working on these days is more maintenance, upgrades, integrity work, more field services type work as opposed to big pipeline projects like we've been executing all over the course of the past year to year-and-a-half. So I'm expecting – that's part of the reason why we're expecting kind of a more normalized run rate on revenue as well as margins over the course of the next few quarters.

Jerry Revich

Analyst, Goldman Sachs & Co. LLC

Q

Okay. We'll see if you can do better than that. Thank you.

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

A

Yeah. Thanks.

Kenneth M. Dodgen

Chief Financial Officer & Executive Vice President, Primoris Services Corp.

A

Thanks.

Operator: Next question comes from the line of Steven Fisher from UBS. Your line is open.

Steven Fisher

Analyst, UBS Securities LLC

Q

Thanks. Good morning. In the...

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

A

Hi Steve.

Steven Fisher

Analyst, UBS Securities LLC

Q

...Utility Segment, you guys mentioned you're starting to see some work ramping back up and will be released in the first quarter of 2022. Can you just give a little more color there? How much work do you think was deferred from the quarter and what's allowing that work to get back up and rolling again?

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

A

Well, again, I think, Steve, and I think some of it's just that the clients have started picking up their pace with respect to releasing work that was slowed for any number of reasons last year that we've discussed, whether it be

the COVID hangover or supply chain or some delays by them and just pausing just to see what the economy was going to do and what COVID was going to do. And I think they're back to normal course of business. We have a number of clients that are looking at their 2022 budgets or trying to finish out this year on projects first of all and finish and complete their spend. But next year, looking at their budgets and knowing what their spend is going to be, trying to ramp up and get prepared to kick off the year on a normal pace, which is quite different than what they were last year.

We also have new work for new clients and new areas with Future and you heard us we referenced those two contracts and there are other projects, too, contracts that we have in not only in Future communications, but in transmission and distribution as well. Those projects will be ramping up towards the end of this year and into next year as well.

Steven Fisher*Analyst, UBS Securities LLC*

Q

Okay. That's helpful. And then on the energy front, I think you mentioned there are some delays in solar, but it doesn't sound like you're too concerned about push-outs or delays or rethinks of projects. What gives you the confidence that that's the case, given all the inflation that we're seeing? Is there a way to maybe bucket the prospects you have in solar, the ones that you know are going to move forward on time, the ones that will possibly move forward on schedule and the ones that you think are most likely to be delayed.

Thomas E. McCormick*President, Chief Executive Officer & Director, Primoris Services Corp.*

A

Well, I don't think I could bucket them for you. I can tell you that our management team is well aware of what the delays are. They are in constant communication with their clients and the suppliers. So, they've kind of baked those delivery schedules into their schedules, and they have actually extended some project schedules to incorporate delays associated with the supply chain. So, we've seen some of these project durations go out longer and you've seen that we've seen the cost of materials and equipment go up and we've incorporated that into our estimates. It's probably – where that will affect us is our estimates or our margins on Renewables projects to be probably closer to traditional, which is roughly, what, 11% to 14% maybe. And you probably won't see those big gains, at least not with respect to buy-down on materials and equipment.

Steven Fisher*Analyst, UBS Securities LLC*

Q

Okay. Thank you very much.

Thomas E. McCormick*President, Chief Executive Officer & Director, Primoris Services Corp.*

A

Thanks, Steve.

Kenneth M. Dodgen*Chief Financial Officer & Executive Vice President, Primoris Services Corp.*

A

Thank you.

Operator: Your next question comes from the line of Julio Romero from Sidoti and Company. Your line is open.

Julio Romero

Analyst, Sidoti & Co. LLC

Hey. Yes. Good morning, Tom and Ken.

Q

Kenneth M. Dodgen

Chief Financial Officer & Executive Vice President, Primoris Services Corp.

Hey. Good morning.

A

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

Hey. Good morning.

A

Julio Romero

Analyst, Sidoti & Co. LLC

Hey. So just following up on Steven's question about Utility work kind of being released soon. I think you mentioned, there was COVID hangover, supply chain delays, et cetera. My question is on the Utility side. Is that work being released that you expect to kind of flow through first half of 2022? Is that related to legacy utilities or more telecom?

Q

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

I think it's actually – it's all of them.

A

Kenneth M. Dodgen

Chief Financial Officer & Executive Vice President, Primoris Services Corp.

Yeah. A lot of it's legacy and it's reflecting the fact that we've been using this year to expand, add new contracts – add new contracts and expand into new geographic areas. And so, we expect some of that start bearing fruit into Q4 and especially into next year.

A

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

[ph] A little bit of both (49:30).

A

Julio Romero

Analyst, Sidoti & Co. LLC

Okay. And it was nice to see Future's gross margins tick up sequentially even with revenue being pulled down a bit. Should we expect to see any leverage on the gross margin line next year as that sales number ramps up a bit or does that kind of 18 percentish gross margin stay steady state and you expect more leverage on the SG&A side?

Q

Kenneth M. Dodgen

Chief Financial Officer & Executive Vice President, Primoris Services Corp.

Yeah. Going into next year I think it's going to be more leverage on the SG&A side. 18% is really what we've been targeting all year long. We knew they could get back to that and sure enough they did this quarter. Depending on the mix of work, I could see the margins possibly getting a little above 18% sometime next year.

A

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

But again, it's really dependent on the mix of work.

A

Kenneth M. Dodgen

Chief Financial Officer & Executive Vice President, Primoris Services Corp.

That's right.

A

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

It really is. And depending on the blend of work they have, if they're in a really dense urban environment, it puts a little pressure on their margins when they get out. And more rural, their margins grow a little bit. Again, it's kind of a mix when you start talking about [indiscernible] (50:38) work. But the 18% is right where we expected them to be and now we just need to get the revenue up. And I'll tell you, 2022 is looking really good not only for them, but for transmission and distribution, and gas will probably be a little bit flat, maybe have some growth in it, probably low single-digits, but their margins are good as well.

A

Julio Romero

Analyst, Sidoti & Co. LLC

Got it. So really just, any benefit to gross margin would be related to mix and not necessarily a ramp up of revenues.

Q

Kenneth M. Dodgen

Chief Financial Officer & Executive Vice President, Primoris Services Corp.

Right.

A

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

Yeah. And I think you're going to see more project work next year, too, which would – typically, you can gain a little bit on your margins there when you successfully execute projects.

A

Julio Romero

Analyst, Sidoti & Co. LLC

Understood. And just if I could sneak one more in here, I think you talked in your prepared remarks about the OSHA mandates and your four-element plan. Can you just kind of sum up what kind of impact vaccination mandates could have on your business if OSHA does require full vaccination?

Q

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

It's hard to speak to if you don't necessarily know what the requirements are. We're following all of the protocols now as far as testing and quarantine and everything else associated with social distancing. And the one thing that OSHA hasn't defined yet is if you're outside, if you typically work outside, are those mandates going to apply? So, if they apply externally, then the implications could be fairly large, although we've been able to adapt, for the most part, over the course of the past two years and haven't really – there have been impacts, but very minor.

A

So I'd like to really see what they're going to do with respect to people that work out – crews that work outside the majority of the time versus office staff. If it's office staff, we can work around it. We'll make it work. If it's crews, then we start getting into, well, what does that look like and how does it impact our labor agreements, how does it impact our contracts. That can be a little bit different deal.

Julio Romero*Analyst, Sidoti & Co. LLC*

Q

Got it. Thanks very much for taking the questions.

Thomas E. McCormick*President, Chief Executive Officer & Director, Primoris Services Corp.*

A

You're welcome. Thank you.

Operator: Next question comes from the line of Matt Sharpe from Morgan Stanley. Your line is open.

Matthew Sharpe*Analyst, Morgan Stanley & Co. LLC*

Q

Tom, Ken, Brook, good morning.

Thomas E. McCormick*President, Chief Executive Officer & Director, Primoris Services Corp.*

A

Good morning.

Kenneth M. Dodgen*Chief Financial Officer & Executive Vice President, Primoris Services Corp.*

A

Good morning.

Matthew Sharpe*Analyst, Morgan Stanley & Co. LLC*

Q

Just want to hit on margins here for a second, specifically sort of the SG&A cost component beyond this year. I think your outlook suggests SG&A will tick down a little bit into 2022 as FIH integration rolls off. Just looking at the current year, if I'd back out FIH, seems to point to about high 5% range similar to 2020. Is there any reason going into next year that you can't sort of beat that level or any other building blocks other than FIH that we need to think about here?

Kenneth M. Dodgen*Chief Financial Officer & Executive Vice President, Primoris Services Corp.*

A

No. Nothing really, Matt. It's really just about continuing to finish the integration of Future, getting their G&A percentage in line with the rest of the company and then just leveraging our revenue growth that we're expecting next year kind of returning to normal without some of the headwinds we saw this year.

Matthew Sharpe*Analyst, Morgan Stanley & Co. LLC*

Q

Got it. Helpful. And then maybe just circling back to CapEx. It looks like you guys raised about \$25 million at the midpoint. I know you noted that there was some acceleration of orders here. Maybe just how much of the

increase was that acceleration? And then given that acceleration, should we expect that 2022 comes down potentially sub 3% or what can you tell us about the trend going forward now that the acceleration is baked into your guide?

Kenneth M. Dodgen

Chief Financial Officer & Executive Vice President, Primoris Services Corp.

A

Yeah. That \$25 million that you're just talking about is really exactly it. That's the addition that we added to kind of get ahead and ready for next year. And then with respect to next year, we haven't finished our CapEx plans for next year. So, lacking any better information, I would say next year is probably going to kind of ballpark where we originally forecasted this year until I have more information.

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

A

In addition to that, we're always going to spend money for growth. So, we'll have a plan. But if there's opportunities for growth, we're going to spend the money. But I agree with Ken. I think this would be more in line with what we forecasted for this year.

Matthew Sharpe

Analyst, Morgan Stanley & Co. LLC

Q

Got it. Thanks, gentlemen. Very helpful. I'll get back in the queue.

Kenneth M. Dodgen

Chief Financial Officer & Executive Vice President, Primoris Services Corp.

A

Thanks, Matt.

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

A

Thanks, Matt.

Operator: [Operator Instructions] There are no further questions at this time. I would like to turn the conference back to Tom McCormick, Chief Executive Officer.

Thomas E. McCormick

President, Chief Executive Officer & Director, Primoris Services Corp.

Thank you, Sarah. I want to thank you for joining us today and close by going back to what I said at the beginning of this call. Our results are a clear evidence of the strength of our overall business and the strategic value of the acquisitions we've made in recent years. We are well-positioned today in the key markets to support our customers and moving toward a zero carbon future. I want to extend my gratitude to our Primoris employees whose skills and hard work form the backbone of our success. Thank you.

Operator: This concludes today's conference call. Thank you for participating. You may now disconnect.

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