

# **Profire Energy, Inc. (PFIE) Q1 2024 Earnings Call Transcript**

Seeking Alpha - Earnings Call Transcripts

May 11, 2024 Saturday

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**Length:** 4835 words

**Byline:** SA Transcripts

**Body**

Profire Energy, Inc. (PFIE)

Q1 2024 Results Conference Call

May 9, 2024 08:30 AM ET

Company Participants

Steven Hooser - Investor Relations

Ryan Oviatt - Co-Chief Executive Officer & Chief Financial Officer

Cameron Tidball - Co-Chief Executive Officer & Co-President

Conference Call Participants

Rob Brown - Lake Street Capital Markets

John Bair - Ascend Advisors

Presentation

Operator

Good afternoon, everyone, and thank you for participating in today's conference call to discuss Profire Energy's First Quarter 2024 Earnings Call.

I will now turn the call over to Steven Hooser, Investor Relations, to get the call started. Thank you.

Steven Hooser

Thank you, operator. With me on the call today is Co-CEO and CFO of Profire Energy, Ryan Oviatt; and Co-CEO, Cameron Tidball. Yesterday, after the market closed, the company filed its Form 10-Q with the SEC and discussed the quarter's highlights in a press release. As always, both of those documents are available on the Investors section of the company's website. The transcript of this call will also be posted in coming days. Before we begin today's call, I would like to take a moment to read the company's safe harbor statement. Statements made during this call that are not historical are forward-looking statements. This call contains forward-looking statements, including, but not limited to, statements regarding the company's expected growth, revenue diversification success, the planned research and development of new products, future projects, future performance in new and existing markets, sales pipeline, potential M&A opportunities and the company's future financial performance.

All such forward-looking statements are subject to uncertainties and changes in circumstances. Forward-looking statements are not guarantees of future results or performance and involve risks, assumptions and uncertainties that could cause actual events or results to differ materially from the events or results described in or anticipated by the forward-looking statements. Factors that could materially affect such forward-looking statements include certain economic, business, public market and regulatory risk factors identified in the company's periodic reports filed with the Securities and Exchange Commission. All forward-looking statements are made pursuant to the safe harbor provision of the Private Securities Litigation Reform Act of 1995.

All forward-looking statements are made only as of the date of the release, and the company assumes no obligation to update forward-looking statements to reflect subsequent events or circumstances, except as required by law. Readers should not place undue reliance on these forward-looking statements. I would like to remind everyone that this call is being recorded and will be available for replay through May 23, 2024. Starting later today. It will be accessible via the link provided in yesterday's press release as well as the company's website at www.profireenergy.com . Following the remarks by Mr. Oviatt and Mr. Tidball, we will open up the call for your questions.

Now I'd like to turn the call over to our Co-CEO and CFO of Profire Energy, Mr. Ryan Oviatt. Ryan?

Ryan Oviatt

Thank you, Steven, and welcome to all of you who are joining us on the call today. Our first quarter results reflect the underlying strength of our legacy business and continued traction with our diversification efforts. Our year-over-year revenue performance declined as we lapped our third best quarterly revenue in company history and saw several significant projects deferred by customers in the subsequent periods. In our view, the near and long-term trends for our legacy business remain highly favorable. E&P companies continue to play catch-up on multiyear deferred maintenance and automation investments. We believe hydrocarbons will continue to play a vital role in global energy production as alternative energy sources will not be fully capable of shouldering the demand load for the foreseeable future. The Biden Administration's January announcement to pause pending and future permits for LNG exports has slowed some industry capital expenditure decisions in recent months and even influenced many natural gas producers to shut off production at existing wells due to the associated drop in natural gas prices.

However, we believe LNG continues to be a key long-term solution for global energy and that North American producers are well positioned to capitalize on this opportunity. As they do so, Profire will continue to be a critical supplier of automation and safety controls for their production infrastructure. The IEA forecast energy demand to increase by 3.5% over the next 3 years versus the low to mid-2% growth rates achieved in 2022 and 2023. This growth will be primarily driven by an increase in overall electrification of world economies, including the massive energy demand increase being required for AI data centers. Morgan Stanley recently predicted that the power demand from generative AI will increase at an annual average of 70% through 2027. These trends and predictions support our belief that we need more of all energy sources, including the ever abundant and reliable fossil fuels. Oil prices rose steadily during the quarter and remained above $80 per barrel, partially driven by supply cuts by OPEC and the ongoing civil unrest in the Middle East.

Recent events have not led to meaningful supply disruptions, but any further escalation and/or broader conflict could have a significant impact on commodity prices and lead to the need for increased North American production. As we have stated previously, we remain very optimistic about Profire's medium- and long-term prospects despite short-term fluctuations in quarterly performance. We believe 2024 will be another strong year for the company with higher revenues and income in the second half of the year. Our strong financial position continues to allow us to evaluate new investment and acquisition opportunities as we move forward with our strategic growth objectives.

With that, let me turn my remarks to Profire's financial results for the first quarter of 2024. During the first quarter, we recognized approximately $13.6 million in revenue compared to $14.5 million in the fourth quarter and $14.7 million in the prior year quarter. Gross profit for the first quarter was $6.8 million compared to $7.8 million in the prior quarter and $7.8 million in the first quarter of 2023. Gross margin was 50% of revenues compared to 54% in the prior quarter and 53% in the first quarter of 2023. The sequential and year-over-year decrease was primarily related to product mix, normal inventory and warranty reserve movements, inflation and the impact lower revenue has on fixed cost coverage within cost of goods sold. Total operating expenses for the first quarter were approximately $5 million or 37% of revenue compared to $5 million or 35% of revenue in the fourth quarter and $4.5 million or 31% of revenue in the year ago quarter. The year-over-year increase reflects the impact of inflation and additional headcount in support of strategic growth and increased business activity.

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Profire's 10-year annual weighted average operating cost as a percent of revenue is 40%, which compared to the performance of the periods noted here indicates that despite inflation challenges, we continue to operate our business in an effective and scalable fashion consistent with growth in activity. Net income for the first quarter was approximately $1.4 million or $0.03 per diluted share. This compares to net income of $2.6 million or $0.05 per diluted share in the first quarter of 2023 and net income of $3.3 million or $0.07 per diluted share in the fourth quarter of last year. As noted on our last earnings call, the lower performance of the current quarter is in large part due to the past several years benefiting significantly from our tax planning efforts regarding deferred taxes, net operating losses in our Canadian subsidiary and employee retention credits in the U.S. Without these efforts, performance in the comparable periods would have been reduced.

Cash used in operations in the first quarter was approximately $2.7 million compared to cash generated of approximately $522,000 in the prior year quarter. This difference was largely driven by the lower net income in the current quarter and necessary increases in inventory as well as reductions in accrued liabilities. Our inventory balance at the end of the quarter was approximately $15.7 million compared to $14.1 million at the end of the fourth quarter. We ended the quarter with $16.2 million in cash and liquid investments and remained debt free.

I will now turn the call over to Cam to provide an overview of our business. Cam?

Cameron Tidball

Thank you, Ryan. As we reflect on our Q1 performance, top line revenue matched our internal expectations. And overall, we are pleased with the results of the quarter. We are excited to report the achievement of our 2 strongest sequential quarters in company history related to total value of sales orders received. Challenging factors facing our traditional upstream business included the warmest winter season on record for the contiguous United States and Canada, reduced drilling and completion activity and lower natural gas commodity prices, resulting in production shut-ins in core gas plays. The industry was also impacted by the over $230 billion spend on mergers and acquisitions from crude oil and natural gas exploration and production companies. Despite these factors, we were able to achieve strong top line revenue and financial metrics ranking amongst our best historically.

The Profire team continues to exemplify our core values and focus on providing performance-driven products and solutions to the energy sector. We remain committed to supporting our customers' goals of reducing emissions, improving workplace safety and optimizing operations through the integration of our proven technology, which provides vital control and automation of their thermal processes and applications. In Q1, we were able to deliver strong combined diversification results, nearly doubling our 2023 Q1 diversified revenue. Our non-oil and gas and industrial revenue nearly tripled compared to the first quarter of 2023. These results are encouraging as we continue to obtain repeat business and find new customers and projects. Our Q1 diversification results were derived from industries, including critical energy infrastructure, landfill, biogas, biofuel operations, refining, power generation and mining. We continue to find new and exciting applications where Profire burner and combustion management technology and expertise can be leveraged.

In the first quarter, we were able to win some exciting new diversification projects, which have the potential to lead to future repeat business. Of note, we were awarded our first project with a leading clean tech and environmental services firm who develops advanced waste-to-energy solutions, integrating Profire burner and combustion management to their proprietary high-temperature pyrolysis technology. Through our combined solution, Woody materials and organic waste can be transformed into renewable natural gas, green hydrogen, syngas as well as valuable biocarbon outputs, including biochar or activated biochar, which is a highly useful filtration media. We believe that we will be able to leverage this opportunity to work with other firms who occupy this space. In the quarter, we were also awarded our third project with an industry-leading biofuel producer. Profire products and solutions match the control needs of this innovator who transformed solid waste into renewable natural gas, which can be used for transportation. We plan to execute on each of these projects in 2024.

In the first quarter, we continued to develop our relationship with a leading OEM who develops direct fired heaters used in a variety of processing plants and petrochemical and refining facilities. As a new customer to Profire in 2023, we are pleased to earn this repeat business as it represents trust in our engineering process and performance of our products. These wins represent a small sample of the progress we are making towards our diversification goals. Our sales pipeline and current backlog in critical energy infrastructure have us on pace to exceed 2023's results in this area of the energy sector. Our non-oil and gas and industrial project pipeline, current sales orders and bid opportunities have us on track to exceed our record-breaking diversification results of 2023. We remain committed to our strategy. We continue to develop our internal teams and individuals, enabling them to provide a customer experience in line with our vision and mission.

Future product development is being shaped by our learnings as we gain insights into new industries and applications we intend to support in the future. As mentioned previously, we feel several factors impacted our ability to deliver results at or exceeding the levels experienced throughout 2023. Warm winter temperatures attributed to an El Nino year impacted natural gas commodity prices as storage was high, and although feedstock demand for LNG remained robust, many producers were forced to shut in production, which, in turn, impacted drilling and completion activity. The record-breaking M&A activity of 2023 slowed project discussions as integration developments impact our customers and their ability to execute purchase orders and make normal operational decisions. Mergers also lead to new contacts, new processes and new software to navigate as part of engineering, procurement and invoicing. We feel that the acquisitions that have occurred will overall be positive for Profire. However, may have some short-term impact or delays as they navigate their integration projects.

As we continue to monitor the health of the energy sector related to hydrocarbon production, demand continues to be strong and is outperforming the narrative generated by the IEA. The ideological battle between OPEC and the IEA regarding global demand for hydrocarbons are trending towards OPEC's analysis currently. In 2023, the U.S. achieved strong growth and record-setting production levels adding over 1 million barrels per day. Consensus remains that U.S. will again achieve production growth in 2024, however, not to the same percentage increase of 2023. We continue to see E&Ps remain disciplined with respect to their capital allocation programs. With an average WTI price of $77.5 in Q1, we believe that the current commodity pricing lies within the price spend, which includes a breakeven point as well as a healthy return to shareholders. Though breakeven points and shale economics have remained relatively stable for the last 4 to 5 years, we have seen a change in the business model.

In addition to returning the cost of capital, the new model includes a return to shareholders. At current prices, we believe we will not see a dramatic increase in rig activity, however, that it will remain stable. We continue to work with U.S. and Canadian majors and independents. Our products continue to support initiatives to help meet Quad-O standards, EPA and Carbon Tax Legislation impacting the energy sector. Profire solutions and service offerings are specified by best-in-class operators, including EQT, Chesapeake, Chevron, Conoco, Southwestern Energy, Vital, CNRL, Cenovus and many others. We support these customers directly or through our numerous valued partners and OEMs. We reaffirm that to meet the world's growing demand for energy, North American produced hydrocarbons are essential and that they have the potential to be the cleanest, most reliable, most ethically produced and affordable means to meet expected growth in demand. We believe that North American producers have and are making incredible improvements to reducing GHG emissions.

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Profire continues to support and be part of this movement in cause. We continue to develop products and solutions for our current traditional markets as well in support of our diversification efforts. Our research and development team has recently been invited to work with a major global E&P on a project that has the potential to evolve the production of oil in the Permian Basin. Though preliminary, we are confident that we can provide value to the project and see future opportunities to collaborate and develop solutions to reduce emissions. Our balanced approach to short-, mid- and long-term product development remains intact. Our focus on M&A activity continues as we follow a methodical process for finding and analyzing opportunities. We continue to look for and meet with companies who we feel have accretive businesses that support Profire's growth and scale initiatives with our current and future markets and customers.

As we look to coming quarters and years, Ryan and I are optimistic and excited about our future. Our traditional customers will continue to automate their new and existing heated appliances. They will continue to look to Profire to enable improvement of efficiencies and lowering their overall GHG emissions, regulations that are in place point to the need for our solutions. Our diversification progress related to burner and combustion management solutions in new industries continues to gain momentum as we prove repeatedly that our over 400 years of combustion experience brings value to several industries and markets. Before we turn to questions, Ryan and I thank you for your interest in and support of Profire. To all of our team members, thank you for all you do to support our customers and our shareholders and each other.

Operator, would you please provide the appropriate instructions so we can get the Q&A started?

Question-and-Answer Session

Operator

[Operator Instructions]. The first question comes from Rob Brown with Lake Street Capital Markets.

Rob Brown

First question on just some of the macro environment, the pluses and minuses, you went through pretty well. Do you expect growth to resume in the legacy business in the back half as these crosscurrents stabilize? Or how do you see this playing out for the next 12 months?

Ryan Oviatt

Our crystal ball is probably as cloudy as yours might be with that regard. But we do think there are a number of things coming into play that point to the fact that it could be better and likely should be better in the second half. As we mentioned, we did have a few projects that pushed out a quarter because of customer preparation, readiness, some issues on their side. So those will come in, in the second quarter or third quarter, potentially. I think most of them are already in the second quarter. But that would have been about another $1 million of revenue that we would have seen in Q1. But on top of that, as we mentioned, that we do think that things are picking back up.

The EIA forecasts a pretty rapid recovery in natural gas prices this summer and heading into next winter, which, again, we don't know what the winter season will be like this coming winter or in the fall. But we think those dynamics combined with ongoing challenges in the Middle East are going to be another means of strengthening commodity prices, which will then have an impact on U.S. producers, their willingness to produce, to continue to invest in their own infrastructure. So yes, overall, we think that things will continue to improve in the coming quarters of this year.

Rob Brown

On the diversification efforts, I think you talked about the doubling of the revenue this year, this quarter and then a sense of a pretty strong sales pipeline, and I know there's a bit of a time line there to get orders in. But could you just characterize the sales pipeline a little more about maybe the size of it and what you're seeing in terms of project activity?

Ryan Oviatt

Yes, certainly. Cam, do you want to give some more color on the diversification efforts in pipeline?

Cameron Tidball

Yes, you bet. As we look at the first quarter, obviously, critical energy infrastructure for us are the downstream side of midstream, those big plants that we've really been working on that leads the charge as an overall percentage because it's just a bigger part of our business so far. And so that really helped us to overall double. When we talk about the non-oil and gas tripling from the year ago quarter, most of the business we're finding for Profire is coming from projects related to things like RNG, renewable natural gas production or methane abatement. And so we're seeing a lot of sources for renewable natural gas coming on, and then it's just like, okay, is that just moving natural gas production around maybe a little bit.

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It's still so very small compared to the overall need for natural gas, but those are new projects for us. But really, the methane abatement, which really hit so many different industries that we're seeing more and more traction, whether it be at landfills, whether it be at agricultural sites or manufacturing facilities. So these are great opportunities for Profire. When we talk about the pipeline, obviously, we don't give out the numbers, but we're very confident, as we said, we believe that we are fully on track to exceed last year's results of diversification. So last year, finishing the year total diversification around that 12% of total revenue, which, again, the top line was our highest ever. We believe that we're going to be able to exceed that. The pipeline is growing with existing customers doing repeat orders, which is a great thing.

It just shows that we're not just one and done projects that we're actually able to deliver some great results. And from that, we're seeing more and more from everything from marketing leads, just the sales team getting more comfortable. The existing non-oil and gas focused team members who are getting more comfortable to be able to take reference cases, the bid pipeline has never been stronger, but some of these projects, as you mentioned, they're longer-term cycle. They can take longer to land, longer to procure design and deliver. But even with those, just with our pipeline right now, we have set the stage with our Q1 performance till to exceed last year.

Rob Brown

Congrats on all on the progress.

Operator

[Operator Instructions]. The next question comes from John Bair with Ascend Advisors.

John Bair

There a couple of Western Canadian pipelines that are ramping up. And I'm just wondering if you're seeing any interest from some of the [Indiscernible] and companies, producers and so forth that are maybe looking to ramp up their production or increase it to help fill those pipelines as we go forward. Can you shed any light on that?

Cameron Tidball

So we have this wonderful anomaly in the Alberta and Saskatchewan markets called spring breakup. Well, with a very odd warm winter and interesting spring, having received snow last week and then it's gone in the 60s and 70s already. But we've seen a shift in the spring breakup period. And obviously, these pipelines coming on board finally, the overpriced pipelines that have been built. We've seen Canada, for the most part; the drilling activity has not gone down as a percentage like the United States. And that's all in anticipation to be able to fill this pipeline. So yes, we do see probably an increase to drilling and activity and production in Canada because with these new accesses to markets, we're seeing an improvement of the -- a lesson of the discount that usually the Western Canadian select hydrocarbon takes in the market because it usually it has to go all the way, sell-through cashing. Now there's access to European and Asian markets through these new pipelines. So yes, in short, we do expect to see a little more activity from players in Canada.

John Bair

So do you anticipate or have you had any indication that maybe there's an increase -- say, existing customers might be increasing their interest in Profire products? Or are there may be some smaller newer or different previously nonexisting customers that might approach you?

Cameron Tidball

The Canada market is obviously our oldest market, and Profire holds a dominant market share here. A lot of the consolidation that we saw in the United States last year has already really occurred in Canada. The players are the players. And I'm sure we'll see some consolidation just for scale and just lowering overall cost. But for the most part, it's existing customers. We know they're just going to pick up activity. There aren't really any new players as per se, but there will be more interest into exploiting existing acreage. Automation strategies are always in place here. They're trying to retrofit things. There are still many, many opportunities left. But yes, really what it comes down to, John would be existing customers doing more than they would when they have a lower per barrel price to work with.

John Bair

And on the regulatory front, are there any new laws in place that would help stimulate for demand for your products for methane capture abatement, that kind of thing?

Cameron Tidball

Yes, that's definitely been a driver really the last couple of years. You've got everything from EPA. You have the inflation Reduction Act, which is moving things there. You have the carbon tax in Canada, which has become more aggressive this year. But companies have really gotten ahead of a lot of these things and just working on the programs because they have so many assets to take care of. Quad O B and C are areas of the United States legislation. It's not so much legislative. Yes, I guess it is, where Profire products and solutions, it points an arrow right at us. It doesn't say Profire, I wish it would, but it does point to what you need to do in terms of not venting methane, raising your efficiencies, complete combustion, all things that Profire is focused on.

John Bair

Last question here. Have you considered or actually reached out to say state department of natural resources that are states with production like here in Ohio, where they're going out and either trying to P&A, orphan wells or monitor methane escape or whatever from older wells or existing wells for that matter and perhaps work with them at all, provide an outlet new customer perhaps? Here in Ohio, we do have a P&A program at the state level and abandoned wells and whatnot. So I don't know exactly how it works as far as the activity that the state undertakes to do that, but it seems that might be an interesting market.

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Cameron Tidball

That's an interesting perspective on it. We certainly haven't done any outreach to specific states or departments of natural resources. But we do have a number of customers that are doing that themselves either for their own wells or coal mines that are being abandoned or shut down or other companies that are doing that on their behalf. So we do have a number of applications where our systems are on methane capture equipment and capture and destruction equipment for those types of resources that are being shut down or mothballed at the end of their lives.

John Bair

No, there's an awful lot of old wells out there. So I would think that might be an interesting area of opportunity.

Cameron Tidball

Well, Ohio is probably at the forefront of tackling the orphan well project. It's the most well-funded. I think there's funding way out into 2035 for that in Ohio. So they're ahead of the game there. But when it comes down to it, as Ryan mentioned, our products and solutions do fit that. And there are many like I'll call them clean tech or capture OEMs, engineering firms that are looking at these problems. You've got several websites like, for example, Naphtha that you can go online and you can see where everything is venting. Sometimes it's a little dated. But as a sales and marketing initiative at Profire, we do look at these things and to see if there is leads that could be generated going directly to the legislative bodies is definitely a challenge, would be a challenge for Profire just to get into the right space. But sometimes we're brought into those conversations just from our customers themselves.

Operator

Ladies and gentlemen, there are no further questions in the queue. I would like to hand the call back to management for closing remarks. Thank you.

Cameron Tidball

Well, thanks, everyone, for joining us on our call today, and thank you, all of you for your continued support. As always, we are available for any discussions or questions you may have. We will also be participating at the Three Part Advisors IDEAS Conference in New York on June 13 and hope to see you there. Thank you, and have a great day.

Operator

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

**Load-Date:** May 12, 2024

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