



**Operator:** Good day, ladies and gentlemen, thank you for standing-by. Welcome to the Pioneer Power Solutions Third Quarter 2013 Financial Results Conference Call. During today's presentation, all parties will be in a listen-only mode. Following the presentation, the conference will be opened for questions. If you have a question, please press the star, followed by the one on your touch-tone phone, and please press star zero, for operator assistance at any time. For participants using speaker equipment, it will be necessary to pick up your handset before making your selection. This conference is being recorded, today, Monday November 11th, 2013.

Now I would like to turn the conference over to Brett Maas of Hayden IR. Please go ahead, sir.

**Brett Maas:** Thank you and good day, and welcome to Pioneer Power Solutions Third Quarter Conference Call. The call today will be hosted by my Nathan Mazurek, Chairman/Chief Executive Officer, and Andrew Minkow, Chief Financial Officer. Following this discussion, there'll be a formal Q&A session open to participants on the call. We appreciate having the opportunity to review the results for the Third Quarter of 2013, and provide an update on the first nine months of 2013.

Before we get started, let me remind you this call is being broadcast over the Internet, and that a recording of the call and the text of management's prepared remarks will be available on the Company's website. During this call, management will be making forward-looking statements. These statements are based on current expectations and assumptions that are subject to risks and uncertainties that could cause actual results to differ materially. Please refer to the cautionary text regarding forward-looking statements contained in the earnings release issued today, and in the posted version of these prepared remarks both of which apply to the content of this call.

I'd now like to turn over the call to Nathan Mazurek, Chairman and CEO for opening comments. Nathan, congratulations on a strong quarter.

**Nathan Mazurek:** Thank you, Brett. Good afternoon everyone and thank you for joining us today for our inaugural conference call as a public company. We have made tremendous progress in the last year and believe it is now appropriate for us to conduct these quarterly calls to discuss our results, and our strategy, as well as to answer any questions from our shareholders. Following my brief overview, I will turn the call over to Andrew Minkow, our Chief Financial Officer, who will cover the details of our financial results. We will then open the call back up for Q&A.

Overall, this was a very strong and productive quarter for Pioneer including several milestone events. Our achievements during the quarter, in brief include the successful completion of the public offering of our common stock including the full exercise of the over-allotment option,



raising a total of approximately \$8 million to fuel our growth initiatives. And uplifting to the NASDAQ Capital Market from the OTC Bulletin Board, and finally the completion of the acquisition of Pico Electrical Equipment in Los Angeles, California in order to form our new division, Pioneer CEP.

Let me focus on the most significant milestone that occurred during the quarter that just ended. We successfully completed a public offering of 1.1 million shares, as well as 165,000 additional shares, which was the full exercise of the over-allotment option granted to the underwriters. The aggregate net proceeds to the Company was approximately \$8 million. We used the proceeds of this offering to repay our outstanding borrowings under a U.S. revolving credit line with BMO Harris Bank, and we expect to use the remaining balance to fund acquisitions, working capital, and other general corporate purposes.

This equity financing has strengthened our balance sheet, has replenished our borrowing capacity, and has given us the flexibility to pursue additional accretive acquisitions that will enhance shareholder value, going-forward. Another significant milestone for the quarter, that followed directly from the capital raise was that our common stock began trading on the NASDAQ Capital Market under the symbol PPSI, and we ceased trading on the OTC Bulletin Board. Again, we see this as another step in increasing shareholder value, as the NASDAQ stock market gives us added visibility, and liquidity within the investment community.

Our third significant milestone during the quarter was the acquisition of select assets from Pico Electrical Equipment Inc., and Pico Metal Products Inc., in order to form Pioneer CEP. Pico historically has been in the business of manufacturing low-voltage switchboards, pedal boards, and custom electrical enclosures, based in the greater Los Angeles Metro area, and primarily serving the robust Southern California market. We expect this acquisition will enhance our product offering, broaden our market opportunities, and our ability to cross sell products and provide operating efficiencies with our other business units.

Since this is our first conference call, earnings conference call, let me take a moment and describe what we do, our growth strategy, and our growth strategy for any investors new to our story. Pioneer Power Solutions is a manufacturer of specialty electrical equipment on related services primarily for the transmission and distribution equipment markets. Our businesses provide highly engineered product solutions for applications in the utility, industrial, and commercial segments of the electrical transmission and distribution industry. Our largest customers include a number of recognized national and regional utilities and industrial companies located in North America. In addition, we sell our products through hundreds of electrical distributors, served by our network of sales representatives in independently operated stocking locations throughout the United States and Canada.



We currently go to market under six principal brands, one, Pioneer Transformers; two, Jefferson Electric; three, Bemag Transformer; four, Pioneer Critical Power; five, Pioneer CEP; and six, under our strategic sales group; we go to market as Pioneer Power Solutions, which is selling products manufactured by each of our business units. Within these core businesses, we design, develop, manufacture, and sell a wide range of electrical transformers and circuit protection equipment used in the control and conditioning of electrical card for critical processes. Our operating subsidiaries distinguish themselves by producing a wide range of engineered-to-order and standard equipment, sold either directly to end-users, through engineering and construction firms or through electrical distributors.

These operating units currently provide a stable platform from which to develop and grow our business lines, revenues, earnings, and ultimately shareholder value. We intend to expand rapidly over the next several years through a two-pronged strategy; first, we are focused on organic growth through continued migration towards more highly engineered products and specialized services, to more fully serve our customers. Second, we intend to pursue additional strategic acquisitions that will provide us with complementary product and service offerings, new sales channels, end-markets, and scalable operations. Hopefully, this brief interview gives you a picture of our business, our strategy, and a view towards our planned execution of these goals.

I will now turn the call over to Andrew Minkow, Our CFO, to provide details of our financial results from our third quarter, and nine months into 2013.

**Andrew Minkow:** Thank you Nathan. This is Andrew Minkow. As Nathan mentioned, this was a strong quarter for us. For the third quarter our revenue was up to 22.4 million, that's an increase of 16.8% or in absolute dollars \$3.2 million, that's up from 19.2 million in Q3 2012.

To break this down further, the \$3.2 million quarter-over-quarter increase includes approximately 2.3 million from our existing operations, and 0.9 million of incremental revenues from our recently acquired businesses; them being Pioneer Critical Power, and Pioneer CEP. Our liquid-filled transformer revenues increased to 11.5 million or a 40.6% increase, from 8.1 million in the year-ago period, this was partially offset by an 8.5% decrease in dry-type transformer sales, to 10.1 million from 11.1 million in the prior year. Our liquid-filled transformer sales benefitted from strong demand by several of our perennial utility customers. The decrease in our dry-type transformer sales was driven mostly by lower sales in the Canadian distributor channel, and to a lesser extent, by lower OEM sales activity.

Our quarterly gross profit was up by approximately 40% to 5.9 million at a 26.3% gross margin, compared to 4.2 million gross profit or a 21.9% gross margin, for the third quarter of 2012. Our gross margin is driven mostly by sales mix, and this quarter was more heavily weighted towards larger custom designed substation-class transformers. Our average gross margin percentage on

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standard dry-type distribution transformers was stable this year's third quarter, as compared to the same period of 2012, and was stable on lower sales volume.

Although still a small contributor in terms of our gross profit dollars, sales of our circuit protection and control equipment, which was mostly in connection with Critical Power projects, had the effect of increasing our consolidated gross margin by 0.4% during the third quarter this year, as compared to last year, which was before we began manufacturing these products. Our selling, general, and administrative expenses were 3.6 million during the quarter or 16.1% of consolidated revenue, compared to 3.2 million or 16.7% of revenues in the year-ago period. The 12% increase in our SG&A absolute dollars was driven primarily by the inclusion of new businesses acquired during 2013, as well as an increase in our corporate expenses.

Our third quarter operating income increased 97% to 2.3 million, up from 1.2 million in the year-ago period. Net income increased to \$1 million, up from 0.2 million in the prior year quarter. Our adjusted EBITDA was 2.7 million, as compared to 1.6 million in Q3 2012. Lastly, for the three-month results, our non-GAAP diluted EPS from continuing operations was \$0.21 per share, up 62% from \$0.13 per share in the comparable prior year period.

Moving on to our nine-month financial results for the period ended September 30th, 2013. Our revenues were \$67 million, up 9.2% or 5.6 million, from 61.4 million in the comparable period of 2012. Breaking this down further, the 5.6 million increase includes approximately 4.2 million from our existing operations, and 1.4 million of incremental revenue from our recently acquired businesses in 2013.

Liquid-filled transformer revenues increased to 33.9 million or a 22% increase from 27.7 million in the year-ago 2012 period. This was partially offset by a 5.6% decrease in dry-type transformer sales, to 31.7 million from 33.6 million. Our liquid-filled transformer sales benefitted from strong demand by several utility customers, and also from users in the oil and gas sectors. The decrease in our dry-type transformer sales was driven mostly by lower sales due to our decision to reduce sales discounts in the Canadian distribution channel, which decreased demand in our view, as well as a large order that occurred in 2012 that was not repeated in 2013.

For the nine months, our gross profit was up 22% to \$16.6 million, at a 24.7% gross margin, compared to \$13.6 million of gross profit or a 22.1% gross margin for the nine months ended September 30th, 2012. Our gross margin is driven by sales mix and we generally achieve higher gross margins from sales of our engineered-to-order products, principally liquid-filled transformers, and systems for Critical Power applications, than we do from the sale of our dry-type transformers.



For the nine months ended September 30th, 2013, as compared to the same nine months of 2012, our liquid-filled transformers represented 50.6% of our consolidated revenue, which is up from 45.2% of our consolidated revenue. Dry-type transformers represented 47.4%, down from 54.8%, and our newest products circuit protection and control equipment; represented 2% of our sales for the nine months ended 2013, up from 0% in 2012.

For the nine months, our SG&A expenses were 10.7 million or 16% of revenues, compared to 9.8 million or 16% of revenues in the year-ago period. The 9.2% increase in our SG&A dollars was driven primarily by the inclusion of the two businesses we acquired during 2013, as well as to an increase in our corporate expenses consisting primarily of higher personnel, and information technology costs, partially offset by lower professional fees.

Our nine-month operating income increased 44.6% to 5.9 million, from 4.0 million in the year-ago period. Net income increased 78.5% to 3.2 million, up from 1.8 million in the prior year period. Our adjusted EBITDA for the nine months was 7.1 million or 10.6% of sales, as compared to 5.4 million or 8.8% of sales in the first three quarters of 2012. Lastly, our non-GAAP diluted EPS from continuing operations was \$0.63, up 37% from \$0.46 in the comparable 2012 period.

Turning our attention to the balance sheet for a moment, our cash and equivalents were 3.3 million at September 30th, 2013, as compared to 0.5 million at December 31, 2012. Stockholders equity, as of the September 2013 quarter, was approximately 29 million, compared to 18 million as of December 31, 2012. Looking at our cash flows for the nine months, net cash provided by operating activities was 3.2 million, compared to net cash used in operating activities of 1.7 million in the year-ago period.

Also, during the nine months ended September 2013, cash provided by financing activities included approximately 7.9 million of net proceeds from the aforementioned public offering of our common stock, offset by 4.3 million of cash used to reduce borrowings under our revolving credit facilities, and to make principal payments on our long-term debt. From a liquidity standpoint, Pioneer is in a very strong position with approximately 12 million of available and undrawn capacity under our revolving credit facilities, which includes the benefits of our cash on-hand.

And finally, one last notable milestone is that we updated our full-year 2013 guidance in August, which was originally issued on April 1st, 2013. Revenue guidance remained unchanged and is expected to be in the range of 89 million to 95 million for the full-year of 2013 including \$2 to \$3 million in circuit protection equipment, and control equipment revenue stemming from the acquisitions we completed in 2013. We increased our guidance for non-GAAP EPS to a range of \$0.80 to \$0.86 per share, which was up from \$0.74 to \$0.80 per share in the original guidance issued April 1, 2013.



This updated guidance does not take into account the additional shares outstanding as a result of the public offering, which was priced on September 18th. Including additional shares from that offering, our revised EPS guidance became \$0.76 to \$0.82 per share. We continue to be enthusiastic about the opportunities we see in all of our markets and the operating leverage we are generating in our business, and this gave us the confidence to make the upward revision in our projection.

This concludes my remarks and I will turn the call back over to Nathan.

**Nathan Mazurek:** Thank you Andrew. In sum, we delivered solid and accelerating financial and operating results for the three and nine months, which included contributions from both of the acquisitions we made in 2013. The significant improvements in operating and net income demonstrate our success to-date in leveraging our business model as our profit growth is increasing faster than revenue growth. And we are maintaining expenses in-line with our revenue growth. We are excited about the opportunities we see in our expanded markets and we are outpacing the average growth rates in our industries.

We are pleased with these results and I want to thank our existing employees, and welcome our new employees who have joined us over the last nine months, for their efforts on behalf of Pioneer Power Solutions. And to those who joined us on the call today, we appreciate your interest in our Company; we thank you for your participation in our first ever conference call and webcast. We look forward to updating you in the coming quarters.

Operator, I'd like for you to turn it over for questions for those on the call. Thank you.

**Operator:** Thank you.

**Nathan Mazurek:** Thank you very much for your time and attention. I look forward to—go, ahead, I'm sorry.

**Operator:** Thank you, sir. We will now begin the question and answer session. Just as a reminder, if you have a question, please press the star, followed by the one on your touch-tone phone. If you would like to withdraw your question, please press the star, followed by the two. And if you are using speaker equipment, you will need to lift the handset before making your selection.

Our first question comes from the line of Philip Shen with Roth Capital Partners. Please go ahead.

**Philip Shen:** Good afternoon, gentlemen, this is Joe Bess asking questions for Phil.

**Nathan Mazurek:** Okay, sure, go ahead Joe.

**Joe Bess:** Can you talk about some of the opportunities you have to cross sell your products into the U.S. and Canada? And will this ability be able to accelerate your growth in 2014? From where you've kind of seen growth rates over the last couple of years?

**Nathan Mazurek:** Right. You know, we always treat cross selling as sort of gravy for us, we never bank on it, we encourage it, but we try not to hang our hat too much on it. This is Nathan, by the way. The cross selling is going better than I personally expected, I'm expecting in 2014, that both Critical Power and CEP will be moving a lot of the transformer, or at least a significant amount of transformer product in the United States for us, which is a very positive thing.

In addition, Critical Power is something that I couldn't have, I did not foresee at all, they're actually moving a significant amount of CEP's products, as an ancillary sort of accommodation they're doing for Critical Power-type customers. So we look at it as that ultimately, that continues and definitely, it's significant enough that we consider it, you know, positive, and something to watch for.

**Andrew Minkow:** And we already have orders of the books today that are cross selling.

**Joe Bess:** Okay. Are you able to quantify at all what the benefit has been so far from cross selling?

**Nathan Mazurek:** Yes, I have to go back, you know, probably in orders we're probably talking a couple hundred thousand dollars, and that's with, you know, CEP was only bought in August and really resurrected or had its catharsis from a business that was really downtrodden. So that in such a short period of time, that's significant for us, and I expect that trend to continue.

**Joe Bess:** Great, okay, and then when we look into 2014 and the growth that you're seeing in liquid transformers versus dry-type, do you see a revenue mix shift happening? And how does this impact your guys' gross margin?

**Nathan Mazurek:** Well, the revenue, you know, shift is the most significant piece. I'm going to let Andrew jump in as well, is probably going to be the growth of Critical Power. You know, Critical Power was coming from zero for us, you know, as compared to 2012. Its 2014 should be well ahead of what it did in 2013. And because those margins are so high relative to everything else, that we're doing or at least relative to everything other than the liquid-filled transformer business, that's going to have a positive impact on the margin. I mean, they had a positive impact on the margins this year and they sold relatively little, but because their gross



margin is so high, it's still impacted profitably the gross margin as a Company. Anything else you want to add?

**Andrew Minkow:** The only I'd add is on the dry-type transformer side, and I think we've made this clear on our public disclosures, we're not looking to grow that by any heroic amount, at least our standard catalogue-type transformers. The margins just aren't as favorable, it's more of a wholesale business. But where we would expect more growth in our transformer businesses for 2014, it would be in what we describe as the power units; these are our custom engineered and manufactured much higher ticket prices. And so that's going to be the growth driver for our dry-type business. Otherwise, you know, I wouldn't expect any sea-shift in our mix between liquid and dry for 2014.

**Joe Bess:** Okay and then, with that the power units, how much better are the margins there versus dry-type? And as that grows, is that also having a positive impact on gross margins from where it is today?

**Nathan Mazurek:** Yes, I mean—do you want to take this?

**Andrew Minkow:** I was going to say they're comparable to our liquid.

**Joe Bess:** Okay, great. Okay, then just a last question. You stated the goal of about a 10% EBITDA margin. Can you give us some additional color on how we get there and how much of this is volume versus pricing?

**Nathan Mazurek:** Yes. I mean, first of all I guess for the year-to-date period, we're already there, right? We're at I think 10.6% year-to-date, and much better than that in the current quarter. The second part of your question was, I'm sorry, you asked me about volume driven versus what?

**Joe Bess:** Looking forward for margin expansion, how much of that will be from volume versus pricing?

**Nathan Mazurek:** I think it's going to be mix more than anything, you know, where the lower margin part of our business, which would be Jefferson, the distribution dry-type, it's that business unit, you know realigning its mix, and really holding the line on not offering any more discounts on just flat out stock-type units, and working harder on the OEM sort of bare magnetic, on the special distribution-type transformers. And that's really where they're going to have the margin improvements, the rest is going to be volume driven by Critical Power, and as Andrew pointed out, more Power dry units where the margins are much more favorable.

**Joe Bess:** Okay, great, thank you for that.





**Operator:** Thank—

**Nathan Mazurek:** Thank you for the question.

**Operator:** Thank you. Ladies and gentlemen, if there are any additional questions, please press the star, followed by the one on your touch-tone phone, at this time. And as a reminder, if you are using speaker equipment, you will need to pick up the handset before making your selection. One moment please.

Our next question comes from the line of John Curti with Singular Research. Please go ahead.

**John Curti:** Good afternoon, gentlemen. My question has to do with your acquisition strategy. You're a relatively small company; the acquisitions you have done to this point are relatively small. What do you see on the landscape out there in terms of additional small companies or companies possibly approaching, you know, your size and doing a more transformative acquisition?

**Nathan Mazurek:** Yes. The real focus now is on the more, I don't know if they're transformative companies as large as us, but our spot that we're looking at is companies maybe doing between \$25 million, \$30 million in revenue. The small acquisitions, the smaller acquisitions would have to be amazingly compelling for us right now, to engage in them. They take a lot of time, we bid them, we got to where we are. We think that moving forward, we need to, we need to push up a little bit higher.

You know, we're experiencing we think enough organic growth and margin improvement that the focus on the acquisitions should be those that really enhance those businesses that are growing fastest, that give us the best chance for long-term margin growth and improvement, and that truly are impactful on the business.

**John Curti:** In many industries, potential acquisition targets come from, you know, kind of small family owned businesses where there's no succession planning or the owner's are just ready to retire, et cetera. Can you kind of talk a little bit about what that landscape looks like for you as you're casting your net about for acquisitions?

**Nathan Mazurek:** Right. I mean, those businesses are definitely out there. You know, we're not familiar with everything, but we do spend a significant amount of time in the industry, we've been in the industry for a long time, our Senior Executives know to be alert for opportunities that come out. So you definitely have that, you have other businesses that were bought by other companies that doesn't fit into their strategies anymore, they're moving in a

particular direction, maybe even higher margin-type growth and faster, is something that we'd be suited to bankroll and are looking to really jettison some of those kinds of businesses.

**Andrew Minkow:** But you're right, for the most part, we're looking at privately companies that have been held through the generations or where, you know, I just look at the portfolio of businesses comprising our groups; they were formally divisions of large companies, now owned by management. In some cases, you know, we also happen upon otherwise really strong businesses in a bad financial situation; we're not timid at that either.

**John Curti:** Then in terms of the ability to continue to move margins higher. Will that come from the two most recent acquisitions; the CEP and I think the other business along with doing more custom manufacturing and design?

**Nathan Mazurek:** Right. So it's definitely going to, you know, CEP will definitely help. We're really looking for the first acquisition, the one done in March, Critical Power, that's in the most exciting and dynamic market that we participate in, and that's where we experience the highest margins. It's where we are offering the highest value proposition, the highest engineered proposition that we as a Company offer and we typically get rewarded for it.

So given that their sales growth is probably going to be faster that's going to be probably more impactful, and as Andrew pointed out earlier, probably the growth of the business we bought two years ago, Bemag, the growth of their power drive business, which is also an engineered product business, which was somewhat dormant for them. The growth of that business only because of its expected sales volume is probably going to be even more impactful. So those two would be the most significant on margins.

**John Curti:** And then with respect to the margins on the two types of transformers you sell. Can you talk about in terms of demand and margin for both of those two types of transformers? What you see going-forward?

**Nathan Mazurek:** Well, let's start with liquid-filled transformers, which, you know, liquid-filled meaning that only a liquid can keep the transformer cool enough for higher voltage-types of electricity transformation. So that's a product that's pretty much going to be limited to utilities, and industrial company substations. So you know, that market is tied to overall industrial growth; it's also tied to the need for utilities to keep their distribution networks operating and reliable. And we've been the beneficiary of that investment over many, many years now.

That's the growth profile for our liquid-filled transformer business. You know, there is—when we look at our dry-type business, there's really I think to make it very simple, there's sort of two segments there. The power dry units we just described, which really have an industrial

application that's not going to be found in, you know, a commercial strip center or some, you know, me too type of building project.

There is an area in which a dry-type power unit could be replaceable or swappable with a liquid-filled where the application might call for one or the other. And so what's driving that business is a lot of it is energy. The mining industry is a good consumer of that type of product. And very large commercial building projects might call for a medium-voltage, dry-type of transformer as well. And then in the distribution dry-type transformer business, you know, that's a catalog product. That's driven by the overall pace of commercial construction.

**John Curti:** And in terms of the differential in the gross margins between the two, what do you kind of see as the trend, going-forward? I mean, are the margins in the two areas relatively stable or have they been under pressure, have they been expanding?

**Andrew Minkow:** I would say the margins are relatively stable in both those segments. So the good news is that they're relatively stable at a higher, well for us at least relatively stable, higher on the power side, only because it's a much more engineered solution. And relatively low stable on the stock units.

**John Curti:** Okay, thank you very much.

**Andrew Minkow:** Pleasure.

**Operator:** Thank you. And there are no further questions at this time. I would like to turn the call back to management for any closing remarks.

**Nathan Mazurek:** Thank you very much to everyone for your time and attention. We look forward to updating you again on our next call. Good evening.

**Operator:** Thank you. Ladies and gentlemen, this concludes the Pioneer Power Solutions Third Quarter 2013 Financial Results Conference Call. We thank you for your participation. You may now disconnect.