Quanta Services (PWR) Earnings Report: Q1 2016 Conference Call Transcript

The following Quanta Services conference call took place on May 5, 2016, 09:00 AM ET. This is a transcript of that earnings call:

Company Participants

- Kip Rupp; Quanta Services, Inc. ; Investor Relations
- Duke Austin; Quanta Services, Inc. ; President & CEO
- Derrick Jensen; Quanta Services, Inc. ; CFO

Other Participants

- Matt Duncan; Stephens Inc.; Analyst
- Tahira Afzal; KeyBanc Capital Markets; Analyst
- Dan Mannes; Avondale Partners; Analyst
- Jamie Cook; Credit Suisse; Analyst
- Noelle Dilts; Stifel Nicolaus; Analyst
- Steven Fisher; UBS; Analyst
- Andy Wittmann; Robert W. Baird & Company, Inc.; Analyst
- Adam Thalhimer; BB&T Capital Markets; Analyst
- Alan Fleming; Citigroup; Analyst
- Chad Dillard; Deutsche Bank; Analyst
- John Rogers; D.A. Davidson & Co.; Analyst
- William Bremer; Maxim Group; Analyst
- Jeff Volshteyn; JPMorgan; Analyst

MANAGEMENT DISCUSSION SECTION

Operator:

Welcome to the Quanta Services first quarter 2016 earnings conference call.

Today's conference is being recorded.

At this time, I would like to turn the conference over to Kip Rupp. Please go ahead

Kip Rupp (Investor Relations):

Thank you, Operator. Welcome, everyone, to the Quanta Services conference call to review first quarter 2016 results.

This call is being webcast, and a replay of today's call will be available on Quanta's website at quantaservices.com shortly after the completion of this call.

Before I turn the call over to management, I have the normal housekeeping details to run through.

Our first quarter earnings release and other information is available in the Investors and Media section of the Quanta Services website, at quantaservices.com.

Following this earnings conference call, we will post in the Investors and Media area of the website summary information that we believe investors may find useful regarding our 2016 outlook.

If you would like to have Quanta news releases and other information emailed to you when they occur, please sign up for email information alerts by going to the Investors and Media section of the Quanta Services website, at quantaservices.com.

You can also access Quanta's latest earnings release and other investor material, such as press releases, SEC filings, presentations, videos, audiocasts, conference calls and stock price information with the Quanta Services Investor Relations app, which is available for iPhone, iPad, and Android mobile devices for free at Apple's App Store and Google Play.

Additionally, investors and others should note that while we announce material financial information and make other public disclosures of information regarding Quanta through SEC filings, press releases and public conference calls, we may also utilize social media to communicate this information.

It is possible that the information we post on social media could be deemed material. Accordingly, we encourage investors, the media, and others interested in our company to follow Quanta and review the information we post on the social media channels listed on our website in the Investors and Media section.

Please remember that information reported on this call speaks only as of today, May 5, 2016, and therefore you are advised that any time-sensitive information may no longer be accurate as of the time of any replay of this call.

This conference call will include forward-looking statements intended to qualify under the safe harbor from liability established by the Private Securities Litigation Reform Act of 1995. These forward-looking statements include all statements reflecting Quanta's expectations, intentions, assumptions or beliefs about future events or performance or that do not solely relate to historical or current facts.

Forward-looking statements involve certain risks, uncertainties and assumptions that are difficult to predict or are beyond Quanta's control, and actual results may differ materially from those expressed or implied in any forward-looking statements.

For additional information concerning some of the uncertainties and assumptions that could affect Quanta's forward-looking statements, please refer to the Company's annual report on Form 10-K for the year ended December 31, 2015, and its other documents filed with the Securities and Exchange Commission, which may be obtained on Quanta's website or through the SEC's website, at SEC.gov.

Management cautions that you should not place undue reliance on Quanta's forward-looking statements and Quanta does not undertake and disclaims any obligation to update or revise any forward-looking statements, based on new information, future events or otherwise, and disclaims any written or oral statements made by any third party regarding the subject matter of this call.

With that, I would now like to turn the call over to Mr. Duke Austin, Quanta's President and CEO. Duke?

Duke Austin (President & CEO):

Thank you, Kip. Good morning, everyone. Welcome to the Quanta Services first quarter 2016 earnings conference call.

On the call, I will provide an operational and strategic overview before turning it over to Derrick Jensen, Quanta's Chief Financial Officer, who will provide a detailed review of our first quarter results. Following Derrick's comments, we welcome your questions.

As many of you know, in March, Jim and our Board of Directors decided the time was right for me to step into the CEO role as part of Quanta's leadership transition planning process. I am humbled and honored by the trust and confidence that they have placed in me with this appointment.

I feel fortunate to transition into the role, following Jim's leadership and strong direction over the past five years. I am the third CEO of Quanta. I've had the privilege to work with great industry leaders over my two decade career. I am fourth generation in the business and began working side-by-side with my father in the field. I've spent the last 15 years of my career at Quanta Services , most recently as Chief Operating Officer. I'll work closely with Jim, Derek and our founder, John Colson, and others to develop Quanta's strategic initiatives. As such, you can expect a continued focus on the operational excellence and building a company for long-term profitable growth.

With that, we will continue to distinguish ourselves through safe execution and best-in-class field leadership. We will pursue opportunities to enhance Quanta's core business and leadership position in the industry and provide innovative solutions to our customers.

We believe Quanta's unique operating model and entrepreneurial mindset will also continue to provide us the foundation to generate long-term value for our customers, stockholders and employees. I look forward to future conversations with you through the year and appreciate your support.

Quanta's first quarter results put us on track to achieve our full-year outlook. Revenues were $1.7 billion for the first quarter. Diluted GAAP and adjusted earnings per share from continuing operations were $0.13 and $0.23, respectively.

While these items declined versus last year's first quarter, which was expected, we ended the quarter with record backlog, which exceeded $10 billion for the first time in the company's history. We believe this bodes well for Quanta as we progress through the year and for the years to come.

For our Electric segment, the volume of larger transmission projects revenues declined quarter over quarter and our Canadian operations are experiencing a challenging operating environment, due to the Canadian economy. Despite these headwinds, our core transmission and distribution operations executed well.

We did incur additional losses on the power plant project in Alaska, which we have spoken about on prior calls. As we entered the testing and commissioning phase of the project, we experienced engineering and production issues that created additional construction costs.

We revised our total estimates on the project to factor in these issues and additional time on the site and recognized these extra costs in the first quarter. Additional resources have been allocated to deliver a quality project to the customer and bring it to scheduled completion.

Although we anticipate putting forth claims for a significant amount of these costs related to these issues, we have not recognized any potential recovery at this point. The project is more than 90% complete and we expect to finish it in the third quarter of this year. These losses were not previously contemplated in our guidance, which highlights the strong performance in our core Transmission and Distribution operations in the first quarter.

With respect to margins, I want to reiterate that we are committed to returning margins to historical levels. However, we are mindful not to compromise our core capabilities and long-term approach to growing the business. We are proactively addressing our margins by adjusting our cost structure, where appropriate, continuing to optimize the use of our equipment resources across the Company, and providing value-added solutions to our customers.

We expect improved Electric segment margins results this year and maintain our positive multi-year outlook on the North American electric transmission and distribution markets. The industry drivers that we have discussed with you over the years remain firmly in place to spur infrastructure investment, such as an aging grid that requires significant investment to maintain reliability, the generation mix shifting to more renewables and natural gas, and the implementation of existing regulations.

We also see several new drivers that we believe will be positive for our industry, such as the extension of the renewable electricity production tax credit, New York's clean energy standard, which calls for 50% of the electricity consumed in the state to come from renewable resources by 2030, and the Canadian government's clean energy initiatives and regional transmission plans.

We believe all of these are significant drivers for new generation sources, which will require greater transmission investment for grid connection in the United States and Canada.

The high-voltage electric transmission award opportunities that we have referenced over the last few quarters are exemplified by our recent contract with Eversource Energy to build a Northern Pass transmission project which was signed in the first quarter.

This project was previously submitted for the New England Clean Energy RFP as part of a competitive process seeking a transmission solution to advance the clean energy goals of Connecticut, Massachusetts and Rhode Island, and to bring clean energy to New England power grid.

If selected, the Northern Pass transmission project will be an approximately 192-mile transmission line that will bring more than 1,000 megawatts of clean, affordable hydro electricity from Canada to New England. This project was not reflected in our backlog at the end of the first quarter.

In addition, our distribution services continued to grow, as our customers increased spending levels to upgrade aging distribution infrastructure and to harden the systems to better withstand extreme weather events.

The electric distribution market has been growing nicely for several years and we believe distribution investment could continue to grow. For example, estimates from the C3 Group call for North American electric distribution construction spending to exceed $35 billion through 2020.

Overall we continue to have a positive long-term outlook for our Electric segment. We will continue to build our base business, while remaining nimble to capitalize on large multi-year project opportunities that develop.

Turning over to our Oil and Gas segment. Revenues and margins were lower this quarter versus the same quarter last year, which was also consistent with our expectations. We expect improved performance for this segment as we move through the year, with the second half of the year being meaningfully stronger than the first half, driven by expected significant increase in large pipeline revenue contributions.

We expect to have a greater number of large pipeline projects in construction this year than any other year since 2010. The large pipeline market is very active, with projects successfully receiving FERC and other approvals and an active bidding and negotiating environment.

In the first quarter, we signed large pipeline contracts for an aggregate contract value of more than $800 million, which we expect to realize this year and next. Looking forward, we continue to work with our customers on additional large pipeline projects and have visibility into significant project activity for the next several years.

In the [natural] gas associated with coal to gas generation switching, natural gas mainline system redundancy and increased natural gas demand, particularly in the Northeast, are all drivers of current natural gas pipeline demand. And as LNG export facilities come online in North America and export volumes increase, we expect additional large pipelines will need to be constructed later in this decade to feed considerable volumes of natural gas to those facilities.

While the LNG market is facing challenges due to low oil prices, it is a market we are watching with cautious optimism. We believe our natural gas distribution and pipeline integrity services have attractive growth opportunities, as well.

The Pipeline and Hazardous Materials Safety Administration, or PHMSA, recently proposed new regulations that should continue to drive multi-year opportunities in the natural gas distribution market, as customer integrity programs continue to accelerate.

And finally, a strength of Quanta is our ability to be opportunistic. One of our strategic initiatives for long-term growth is to find adjacent market and new market opportunities. Over the past several years, we have been growing our telecom infrastructure services operations in Canada by leveraging our electric power services resources, reputation and relationships.

We have also successfully greenfielded and grown our telecom infrastructure services operations in various Latin American operations. You may recall from our fourth quarter earnings call that we were recently awarded two sizable telecom concession projects in Latin America. We hope to leverage our telecom success in Latin America into the electric power and other infrastructure service opportunities in that region.

Following the expiration of our telecom non-compete arrangement, a natural progression of these efforts, and our success will be to expand our operations in the US telecom infrastructure services market, which we believe offers a significant long-term growth opportunities. We will currently perform limited telecom-related infrastructure services in the US, consistent with what is permitted by the terms of our non-compete arrangement. I am not going to go into detail about our strategy to return to the market today, but once our non-compete arrangement expires later this year, we envision growing our telecom infrastructure services business in the United States.

In summary, we expect a significant increase in activity levels in the second half of the year and are on track to achieve our full-year outlook. We continue to have a positive multi-year view on the end markets we serve and believe we are well positioned to serve the expanding needs of our customers.

Quanta's entrepreneurial business model is unique and a critical driver of our success. We believe we have the best leadership and the best skilled work force in the markets we serve. The combination of acquisitions and organic growth has allowed us to build a nimble company with a comprehensive breadth of self-performed infrastructure solutions, which significantly distinguishes us in the marketplace.

All of this positions us to generate long-term shareholder value, while maintaining the core values that have served us well through changing market conditions.

With that, I will now turn the call over to Derrick Jensen, our CFO, for his review of the first quarter results. Derrick?

Derrick Jensen (CFO):

Thank you, Duke. Good morning, everyone.

Today we announced revenues of $1.71 billion for the first quarter of 2016, compared to $1.86 billion in the prior year's first quarter. Net income from continuing operations was $20.5 million, or $0.13 tax per diluted share.

These results compared to net income from continuing operations of $47.7 million, or $0.22 per diluted share, in the first quarter of 2015. Adjusted diluted earnings per share from continuing operations, as presented in today's press release, was $0.23 for the first quarter of 2016, as compared to $0.28 for the first quarter of 2015.

The decrease in consolidated revenues in the first quarter of 2016 as compared to the same quarter of last year was primarily a result of fewer ongoing larger electric transmission and large diameter pipeline projects in the current quarter, resulting mainly from fluctuations in project timing and regulatory delays on certain mainline pipe projects and, to a lesser extent, from reduced demand for services, due to lower oil prices and their impact on customer spending.

In addition, consolidated revenues were negatively impacted by approximately $32 million, or 1.9%, compared to the first quarter of 2015, when quantifying the estimated impact of changes in foreign exchange rates between the quarters. Partially offsetting these decreases was the favorable impact of approximately $30 million in revenues generated by acquired companies, primarily in our Electric Power Infrastructure Services segment.

Our consolidated gross margin was 11.9% in the first quarter of 2016, as compared to 12.8% in the first quarter of 2015. This decrease was primarily due to increased costs associated with continued engineering and production issues on a power plant construction project in Alaska that resulted in $21.3 million of project losses recorded during the first quarter of 2016, and the previously mentioned decrease in revenues from large electric transmission and mainline pipe projects, which typically yield higher margins.

Selling general and administrative expenses were $158.5 million in the first quarter of 2016, reflecting an increase of $13.1 million as compared to the first quarter of 2015. This increase was primarily attributable to severance costs associated with the departure of Quanta's former President and Chief Executive Officer, as well as severance and restructuring costs associated with certain operations, primarily in the Oil and Gas segment, which totaled approximately $6.3 million.

In addition, increases were from $3.6 million in incremental general and administrative costs associated with acquired companies and $3.6 million in higher salaries and benefits costs, largely associated with cost-of-living increases. Selling, general and administrative expenses as a percentage of revenues were 9.3% in the first quarter of 2016, as compared to 7.8% in the first quarter of 2015. This increase was primarily due to the impact of the severance and restructuring costs mentioned previously, as well as reduced revenues for the first quarter of 2016.

To further discuss our segment results, Electric Power revenues were $1.19 billion, reflecting a decrease of $53.3 million quarter over quarter, or approximately 4.3%.

Quarter-over-quarter revenues were adversely impacted by reduced customer spending, primarily associated with large electric transmission projects. Foreign currency exchange rates also negatively impacted first quarter 2016 revenues in the segment by approximately $18 million.

These negative factors were partially offset by the contribution of approximately $25 million in revenues from acquired companies and approximately $12 million in higher emergency and restoration services revenues.

Operating margin in the Electric Power segment decreased to 7.4% in the first quarter of 2016, as compared to 8.8% in last year's first quarter. This decrease was due to increased costs on the power plant project in Alaska during the first quarter of 2016.

In addition, the decrease in revenues from the large electric transmission projects mentioned previously negatively impacted this segment's margins, as our revenue mix shifted to a higher proportion of smaller scale transmission work.

Although we experienced strong execution on transmission work overall this quarter, this change in revenue mix inherently carries a higher degree of inefficiencies associated with transitioning between smaller projects that are not experienced during continuous production on larger projects, as well as certain large transmission resources being underutilized during the first quarter of 2016.

As of March 31, 2016, 12-month backlog for the Electric Power segment decreased by 1.4% and total backlog increased 1.4% when compared to December 31, 2015. The increase in total backlog was largely attributable to approximately $90 million of favorable changes in currency rates.

Oil and Gas segment revenues decreased quarter over quarter by $94.4 million, or 15.2%, to $526.7 million in the first quarter of 2016.

This decrease is primarily a result of fluctuations in large project timing, regulatory delays on certain large mainline pipe projects, and to a lesser extent, reduced demand for services due to lower oil prices and their impact on customer spending.

Segment revenues contributed from our international operations were negatively impacted by approximately $14 million as a result of less favorable foreign currency exchange rates in the first quarter of 2016 as compared to the first quarter of 2015.

Operating income for the Oil and Gas segment as a percentage of revenues decreased to 1.1% in 1Q 2016 from 3.9% in 1Q 2015. This decrease in operating income as a percentage of revenues was primarily due to the decreases in revenues from large diameter pipeline projects, which typically carry higher margins, the impact of lower overall revenues reported by the segment, which negatively impacted this segment's ability to cover fixed and overhead costs, as well as the impact of approximately $2 million in severance and restructuring costs.

12-month backlog for the Oil and Gas segment increased by $584.5 million, or 30.8%, and total backlog increased $608.2 million, or 19.8%, when compared to December 31, 2015. These increases were due to the award of several large diameter gas transmission projects during the quarter.

It is worth noting that as a result of these awards, as of the end of the first quarter, the midpoint of our annual revenue guidance does not include any uncommitted revenues associated with large diameter pipeline projects.

Corporate and non-allocated costs increased to $6.9 million in the first quarter of 2016 as compared to 1Q 2015, primarily as a result of $4 million in costs associated with the departure of Quanta's former President and Chief Executive Officer.

For the first quarter of 2016, operating cash flow from continuing operations provided approximately $199.7 million and net capital expenditures were approximately $42.6 million, resulting in approximately $157.1 million of free cash flow, as compared to free cash flow of approximately $122.4 million for the first quarter of 2015.

Free cash flow for the quarter of 2016 was positively impacted by lower working capital requirements, due to fewer ongoing large electric transmission and large diameter pipeline projects in the quarter.

DSOs were 76 days at March 31, 2016, compared to 75 days at December 31, 2015 and 84 days at March 31, 2015. DSOs were lower at March 31, 2016 compared to March 31, 2015, primarily due to favorable billing terms for certain large projects ongoing in 2016.

Investing cash flows of continuing operations during the first quarter of 2016 were impacted by aggregate cash consideration paid of approximately $39.7 million net of cash acquired related to the closing of three acquisitions during the quarter. Financing cash flows of continuing operations during the first quarter of 2016 were impacted by net repayments of $75.2 million under our credit facility.

At March 31, 2016, we had approximately $155.3 million in cash. At the end of the quarter, we had about $321.1 million in letters of credit and bank guarantees outstanding to secure our casualty insurance program and other contractual commitments, and we had $397.7 million of borrowings outstanding under our credit facility, leaving us with approximately $1.25 billion in total liquidity as of March 31, 2016.

As previously mentioned in our fourth quarter earnings release call, we only provide annual guidance and will adjust our expectations as we move through the year, if needed. For the year ending 2016, we expect consolidated revenues to range between $7.5 billion and $8 billion.

This range contemplates Electric Power segment revenues ranging from a decline of around 5% year-over-year at the low end of our guidance to revenues in the segment remaining flat at the higher end of our estimates, with the remaining difference in revenues coming from growth in the Oil and Gas segment.

As it relates to seasonality, I would generally assume usual seasonality through the year, with the first quarter being the lowest with respect to consolidated revenues and margins. We continue to expect revenue and margin improvement sequentially in the second quarter and again in the third quarter, with the third quarter expected to be the strongest quarter of the year.

I would assume revenues and margins in the fourth quarter to fall somewhere between that of the second and third quarter, and that overall, the second half of the year to be more heavily weighted than the first half of the year.

Consistent with our previous guidance commentary, we expect a more pronounced difference between the quarters of 2016 than we have experienced in recent years. We expect a sizable ramp up in revenues through the third quarter, as we expect a significant number of large pipeline projects to begin moving to construction in the second and third quarters of this year.

Fort 2016, we believe margins will continue to be at levels lower than our historical expectations, with the Electric Power segment margins somewhere in the 8% to 9% range and Oil and Gas segment margins between 5.5% and 7%. In addition, largely due to ramp up in revenues I spoke of earlier, we expect margins to reflect a fair degree of seasonality, with a more pronounced effect through the year in Oil and Gas segment, due largely to the anticipated timing of large pipeline project starts.

We estimate that interest expense will be between $15 million and $20 million for 2016 and are currently projecting our GAAP tax rate for 2016 to be between 36.5% and 37.5%. Also, our annual 2016 guidance reflects the current foreign exchange rate environment. Continued movement of foreign exchange rates in the future could make comparisons to prior periods difficult and could cause actual financial results to differ from guidance.

For purposes of calculating diluted earnings per share for the year ended 2016, we are assuming 156.9 million weighted average shares outstanding. Consistent with our previous guidance, our estimates include the reduction of shares in April, 2016 associated with the final settlement of the shares delivered under the ASR program. The actual shares delivered as part of that settlement was approximately 9.4 million shares. This brings the total shares retired under the arrangement to 35.1 million shares at an average price of $21.36.

In total, under our previously authorized $1.25 billion share repurchase program, we have acquired $1.2 billion of stock at an average of $22.10. Under the current and most previously completed share repurchase programs, we have now repurchased approximately $1.7 billion, or 71.7 million shares of our common stock.

This has reduced our shares outstanding by approximately 32% and reduced them to the level we last had almost a decade ago. This while Quanta is now nearly 4 times the revenues of our Company back then and while maintaining a current leverage profile of less than 1 turn of EBITDA. We would intend to use the remaining $50 million available under our 2015 program to repurchase additional shares opportunistically, depending on the overall capital needs of the Company.

In spite of the incremental project loss recorded during the first quarter, we continue to anticipate GAAP diluted earnings per share from continuing operations for the year to be between $1.30 and $1.50 and anticipate non-GAAP adjusted diluted earnings per share from continuing operations to be between $1.61 to $1.81.

Our forecast non-GAAP measures are estimated on a basis similar to the calculations of historical adjusted diluted earnings per share from continuing operations presented in our release.

CapEx for all of 2016 should be approximately $200 million to $220 million. This compares to CapEx for all of 2015 of $210 million.

We expect to continue to maintain our strong balance sheet and financial flexibility, positioning the Company for continued internal growth and the ability to execute on strategic initiatives. Overall, our capital priorities remain the same, with a focus on ensuring adequate resources for working capital and capital expenditure growth and an opportunistic approach towards acquisitions, investments, and the repurchase of Quanta stock.

Lastly, I worked closely with Jim throughout his entire 17-year career at Quanta, and we all want to thank him for his many and significant contributions. Through his years here, he helped put in place much of the foundation that made this organization a success. He was a valued leader and we all wish him well.

Jim and Duke forever worked as a team, such that for us, the transition to Duke as our CEO is natural, anticipated, and supported by our entire organization and we look forward to many successful years with his leadership. This concludes our formal presentation and we will now open the line for Q&A.

Operator?

QUESTIONS & ANSWERS

Operator:

(Operator Instructions)

Matt Duncan, Stephens.

Matt Duncan (Analyst - Stephens Inc.):

So the first question I've got is on the Oil and Gas segment. You guys obviously had a great bookings quarter there and I think if I heard you correctly, you don't need any more bookings there to get to the midpoint of the revenue guide. But how are you expecting backlog to trend there over the balance of the year? Are you still seeing enough work that you think you can continue to grow that backlog level, even as you work off the high level of backlog you've got there now?

Duke Austin (President & CEO):

Yes, Matt. This is Duke. I think, again, backlog, the way it takes us a while to negotiate some of these larger projects, so I don't want to comment on exactly when backlog will come in. It's a robust environment, bidding environment on large pipe, as well as other MSAs in the Gas segment. And I think we'll continue to be opportunistic there and able to book work. I just don't know the timing on it as we move forward through the year.

Matt Duncan (Analyst - Stephens Inc.):

Okay. No worries. In Electrical, if you take out the Alaska charge, the $21.3 million, it looks like that margin would have been about 9.2% this quarter. That's the highest margin I think you would've had since the first quarter of 2014. I'm just curious how you think it's going to trend from here over the balance of the year and what you guys have been doing on the cost side to try and get the margins back into your historical target range?

Derrick Jensen (CFO):

Yes. From a trend perspective, I think what we look at is that inclusive of the charge, that you'd have margins progressing through the year. You're right that the first quarter margins without that charge are higher. We had some actually good weather this quarter throughout, had very good production on a number of projects, transmission and distribution wise. So that did come in a little bit higher than what we would have thought or had expected for the first quarter. In general, we're going to stick with our overall 8% to 9% for the year, because as we move forward through the year, we still have some of the pressure of lower contributions of large transmission work as compared to 2015.

Duke Austin (President & CEO):

And also Matt, the breakup in Canada in the second quarter is obviously something that we'll take into account. And the more pronounced Canadian economy being down will affect us there in that second quarter. So it will be more pronounced in the second quarter. But again, our goal is to get the 10% to 12% range in the Electric Power segment over time.

Operator:

Tahira Afzal, KeyBanc Capital.

Tahira Afzal (Analyst - KeyBanc Capital Markets):

Congrats on a decent quarter. First question, Duke, when I take all of what Derrick has said and put it together, it seems like potentially if things go as planned, your third quarter could probably be the strongest cash EPS quarter you've seen?

Duke Austin (President & CEO):

Tahira, I think that's correct. Again, there's the projects, and it's definitely in the later half, depending on where the projects go. The third quarter, yes, it's setting up to be the biggest quarter.

Tahira Afzal (Analyst - KeyBanc Capital Markets):

Got it. Okay. And then Duke, you talked a little more about telecom and there was some other news that came out this morning. Can you elaborate on what you are seeing there that's really making you jump in? You just got out of the sector a bit back and now it seems you guys are interested again.

Duke Austin (President & CEO):

Tahira, I don't really want to comment a lot about it, other than to say what we said in our prepared remarks is that we're in the business in Latin America and in Canada and stayed that way. And so as far as the strategy going forward, we'll update you as we go forward.

But in general, we're always opportunistic around things -- or in line adjacent to what we do. And that certainly is something that's adjacent to our markets we serve in different areas. Again, and as far as what was said, really have no idea other than to say that there is a public statement out there that has our whole buy-sell agreement in a website. So everyone can turn to that to look at what it says.

Operator:

Dan Mannes, Avondale.

Dan Mannes (Analyst - Avondale Partners):

First, Duke, congrats on the promotion. And then secondly, first, on the Oil and Gas business, you guys booked some pretty good mainline work that it sounds like is heavily towards 2016. Can you contrast that booking with the guidance? Was there any thought -- did this just fill the gap, or can you walk us through maybe your thought process on why this didn't even push guidance a little bit higher? Or is that due to the Electric side?

Derrick Jensen (CFO):

Yes, Dan. If you recall in our last conference call, we talked about we had anticipated some of these awards to come through to fill the gap. And this is actually the closure of that. So it did just effectively fill the gap. We have no uncommitted large diameter work in our current forecast, as it relates to meeting the mid-point. And then some of these projects still yet roll over into 2017. Only roughly a little over half of it is contributing to 2016.

So as it stands here today, we're not looking at doing anything from a guidance perspective. To a great extent, we continue to be cautious about how the timing of these projects will go, and mainly associated with potential delays and we're definitely trying to take that into consideration overall relative to our expectations.

Duke Austin (President & CEO):

And again, we continue to look at throughout 2016, we're not stopping, from that standpoint. We continue to bid and negotiate and look at work in 2016. But like Derrick said, that should fill up what we said we would do.

Dan Mannes (Analyst - Avondale Partners):

Got it. And then the follow-up question is really related to your capacity. Given the amount that you've already booked, how much room do you have to add more work, and if you can contrast that US versus Canada, for the balance of 2016?

Derrick Jensen (CFO):

Yes, we have capacity, Dan. We're not at capacity on either side of it. Canada is probably softer than the lower 48, at this point, in Gas. But we still have some room to book. We'll be cautious about how we go about it and where it's at. And again, the way the regulations are working with the state and federal getting involved in all these larger projects, we're pretty cognizant about how we talk about it.

Operator:

Jamie Cook.

Jamie Cook (Analyst - Credit Suisse):

Hello. I guess two questions. One just broadly on your margins assumption for 2016. If I look at Electric Power, you mentioned another award that you booked which wasn't in the first quarter backlog. Your margins ex the project were again at the higher end of what you're targeting for the year. If I look at the Oil and Gas business, recognizing the first quarter margins were weak, but we expected that, the bookings that you put up in the quarter and what appears to will happen throughout the year are pretty good. I'm just trying to understand why margins couldn't potentially be higher, given the bookings that we have and the underlying profitability of the business. So is it still uncertain, while you've booked things, on timing? Is the pricing environment more competitive so the stuff that we're booking is lower margin? I'm just trying to get a feel for why margins broadly couldn't potentially be higher, because the bookings are there, unless there's other projects that we're concerned about.

And then my second question, Duke, is a question to you more strategically. Back to the telecom business, while you can't give us your exact plan, as you're refocusing on the telecom business, do we read that as potentially longer term or an 18-month, you're not as optimistic about the growth opportunities that the Electric Power or the Oil and Gas business can generate? I'm just trying to think, is this incremental or is this a diversification strategy because you see one of the other businesses tapering out? Thank you.

Duke Austin (President & CEO):

I'll take the last one first and just say, in general, we're always looking at adjacent markets and markets that our customers are driving us towards. We feel like anything that we're going forward with would be an adjacent market or something that's strategic to us. We've stated many times that if we're going in something, we think it has the ability to be a $1 billion business as we look long term. And again, anything you see us doing, that's where we're going. And we don't want to get too far on the strategy on any certain one of them, but that is certainly something that we're looking at to grow us into the future.

As far as our end markets, our end markets that we're currently in today are robust. We are in the telecom market in Latin America and Canada and it's a good market there, as well. So our end markets today are robust. And we're very happy with where we're at. And anything that we're doing on the outside of that is additive and adjacent and strategic to us as we grow the business out in the long term. As far as what's in backlog and where that's at and our margins for the rest of the year, I'm going to let Derrick answer that.

Derrick Jensen (CFO):

Jamie, overall, more specifically, I'll start with Electric Power, we're seeing a lower margin profile, but it has nothing to do with the bidding environment or the way we're approaching bidding. Our margins in backlog from a bidding perspective are comparable to what you've seen in the past. What you've got, though, is as we face the rest of 2016, you have a lower contribution of on larger transmission work. And those carry higher margins. So you have a higher complement of the smaller transmission work, which bears a little bit lower margin. And then in addition, the Canadian economy overall has put pressure on the margins in the Electric side there and we're factoring that into our expectations for 2016. So it's not a pricing or a bidding environment for us. It's really just the complement of the work that's contributing to the 2016 versus what you've seen in the recent past.

Also actually, you made reference to the project that we announced that is not in backlog. At this stage in the game, that's also not in our expectations, because it's not in backlog either at March 31 or in the second quarter. We have not placed that project in backlog at all as of yet.

And still, then relative to the pipeline side, we're mobilizing on a lot of jobs all at the same time here into the second and third quarter. And to that end, that bears a degree of risk and we've tried to take that into consideration in our margin expectations. Mobilizing on that much work, you want to be prudent in how you think about the execution profile of that.

Lastly, as you mentioned, there is a degree of the timing of when that work falls. We try to be prudent with that, looking at how in the past we've had projects move from one quarter to another for some delays, inclusive of the fact that we anticipate some risk that projects could move, to a certain extent, from 2016 into 2017. So we've tried to be prudent across both of those to take into consideration the environment we're working in.

Operator:

Noelle Dilts, Stifel.

Noelle Dilts (Analyst - Stifel Nicolaus):

First, on the transmission market and addressing the shift in terms of the mix that you're seeing in terms of large versus small projects. When you look forward, when I look at the transmission market, it seems like we're starting to see fewer but larger projects out there on the horizon, and it also seems like there's a bit of a trend where some of the project developers are shifting or splitting up some of the larger projects into smaller pieces. As you look forward, do you think we're going to see a rebound in large project work or do you think that shift toward smaller project work is going to be around for a couple of years?

Duke Austin (President & CEO):

As we look at the electric transmission market, we see the opportunity on these larger projects. They are there. How they go about executing them, as far as from small to large, it's really customer driven. It's all over the place on that. Again, we look at it on all sorts of ways as far as that goes. But our capital budgets that our core customers in the market and IOUs continue to grow. We continue to see demand in that market. And from our standpoint, we see it long-term.

The transmission backbone is aging. The way you're bringing renewables on and the way you need to move power across the US is certainly a demand for transmission. So we'll take advantage of small or large. The projects are there. We're going to adhere to our bidding profiles that we have in the past, which we won't win them all. So again, I think there's risk to the projects. We take that into account when we're bidding this work. And so we won't win all these larger projects, but there is the opportunity for us to win our fair share. We like the market, as we go forward, on the transmission side.

Noelle Dilts (Analyst - Stifel Nicolaus):

Okay. And then in Oil in Gas, I think on the fourth quarter call, you talked a bit about the gathering and smaller project work that you're doing in the Marcellus being down maybe on the order of 50%. Can you talk about if that's tracking in line with your expectations and how you're thinking about gathering work moving forward? Have we essentially bottomed in that market yet?

Duke Austin (President & CEO):

Yes. For the most part, we participated in the gathering market in Canada and the Marcellus. So we don't feel the major effects of all the shells being down. But for what we did do in the Marcellus, it is off some, but certainly offset by the larger Diamond pipe moving gas through redundancy on your gas side, as well as just moving it across the Northeast. And in Canada, we do have some projects there moving gas, as well. While it is off some, I think the larger Diamond pipe offsets that.

Operator:

Steven Fisher.

Steven Fisher (Analyst - UBS):

Congrats, Duke. There were some big developments at Nalcor recently. Can you just talk about those two projects? Are you guys on track from a cost and timing perspective? How big a risk is there that as your work is forced to slow down or maybe your inflow of cash payment gets disrupted at all by the whole rethink of the major projects there?

Duke Austin (President & CEO):

Yes, Steve, we're well into the project. And so we have not seen anything on the ground there that would make us think that the project would be canceled or delayed. We continue, the material is there, the right-of-way is certainly getting cleared as we go forward. So I don't see any kind of disruption on Nalcor. It is remote. There is a lot of press in Newfoundland. So again, we are cognizant of that. We're working with the project team, and also we will be working with the new CEO as he comes in to make sure that we're both on the same page. And as far as where we're at, we're comfortable with our estimates on the project.

Steven Fisher (Analyst - UBS):

Okay. That's helpful. You mentioned Northern Pass and a few positive developments in transmission. I know you've talked about this a few times on the call already. But to what extent has your view of the revenue growth potential of the transmission business changed over the last, say, few months? Are you now more positive about this being a growth business over the next 12 to 24 months? Are you the same, less so? How's your view on the transmission market changed just in the last few months?

Duke Austin (President & CEO):

I think the need for transmission remains, both in the lower 48 and Canada, especially when you tie in renewables and you need the backbone of natural gas. So the need is there. How the projects get developed and how they get out and when is the key to it. I think we're following all those larger projects, as well as the underlying need for the smaller transmission coming off the backbone, as well. It's there. It's just how also the economy affects some of that smaller transmission, as well. So you have to take all those things to account.

Saying all that, I would say we're optimistic that the end markets transmission will be back and the larger transmissions will be back as we go forward. If not, we'll adjust our cost. And again, historically we can remain in the 10% to 12% range for the long term and we view it a long-term business and we will be in that range long term.

Operator:

Andy Wittmann, Robert W. Baird.

Andy Wittmann (Analyst - Robert W. Baird & Company, Inc.):

Just wanted to talk a little bit more on Steve's earlier question about some of the Canadian projects. But you had the Fort McMurray West project with Adco that was supposed to start sometime next year. With some of the softening in the Canadian market that you referred to, is that one still on track to start up, as well? What's the status of that $1 billion project?

Duke Austin (President & CEO):

So we work with the [HO] there, who is our client, on that project. And we're meeting with them regularly, monthly. And we feel like the project's on track to go. It may expedite a little bit. But as far as we're concerned, it's on track and everything that they're telling us, there's a need for the reliability in Alberta. So we will be getting started on that here later in the year or early 2017.

Andy Wittmann (Analyst - Robert W. Baird & Company, Inc.):

Okay. And there was an announcement of a fairly large privately held pipeline company that actually filed for bankruptcy. Are you seeing stress from your competitors that maybe don't have the exposures that you have that are an opportunity for you to maybe move into some geographies where you weren't or maybe pick up some assets in M&A at a discount. I guess the question is, how much disruption is out there? Is this the first of many? Is this unusual? And what's the implication for your business?

Duke Austin (President & CEO):

Yes. I don't want to comment on our competitors. Obviously, that's in the marketplace and everyone knows what's out there. What I will say is that the capital markets are there. We're talking to all of our customers about solutions. The risk of large diameter pipe is certainly evident in there and we understand that. When we acquired Price Gregory, we acquired them for that reason, their expertise in large diameter pipe and the risk associated with it. We feel like we've got the very best management team you can get in that area and mitigated those risks and feel confident in our ability to execute on large pipeline projects. As far as the risk that others are willing to take, we can't control that.

Operator:

Adam Thalhimer, BB&T Capital.

Adam Thalhimer (Analyst - BB&T Capital Markets):

On telecom, historically the margins there were a little bit consistently lower than T&D. And I'm just wondering if versus four or five years ago, has the industry changed at all? Do you think you can generate higher margins there going forward?

Duke Austin (President & CEO):

Anything, any business that we do adjacently we'll take the margins into account and make sure that they [inherited] what we believe appropriate for the risk we take, as well as our capital. So we'll take in those accounts when we look at any markets we're in. So if we move into that market, we would look at those things before we moved.

Adam Thalhimer (Analyst - BB&T Capital Markets):

Okay. And I wanted to ask on the transmission side, previously you've talked about FERC 1000 being a driver and maybe even a driver for projects specifically in 2017. Is that still how you look at FERC 1000?

Duke Austin (President & CEO):

With I would say about FERC 1000 is in general, is it gets a lot of press. It's more about merchant transmission, I would say, and just to say that there's a lot of things going on within our industry around merchant transmission and whether they go or not is very difficult. We're around the edges on all those large transmission jobs. We're involved in them, we see them. But again, it's our core business we're focused on on a day-to-day basis and driving margin to our core business, and that's what we are focused on, while we are around the edges on all the rest. And the markets are good with or without FERC 1000.

Operator:

Andrew Kaplowitz, Citigroup .

Alan Fleming (Analyst - Citigroup):

It's Alan Fleming on this morning, in for Andy. Duke, have you seen any change in the bidding environment in oil and gas over the last couple months, with the rise in oil prices, and has the tightening in mainline industry had any impact on pricing or terms and conditions yet?

Duke Austin (President & CEO):

Yes. So natural gas, what we're really seeing is in natural gas removing natural gas. And it doesn't have anything to do with the price of oil, in our mind. For redundancy to export LNG in places, various things, Northeast you're going to have to have backbone gas to support your renewable infrastructure, and so that gas, the movement of it, is going to be there. It's economical, and so we'll continue to see that movement.

And as anything when you get constrained, the market gets constrained at what you can do and the people that can do it, obviously the terms get better. We try to take a fair approach with the customer in good and bad times and negotiate a fair contract for us both and get the right kind of risk associated with it in any contract we look at. But we're in this for the long term. We want to be in here forever, so again, we take that into account when we look at these contracts.

Alan Fleming (Analyst - Citigroup):

Okay. Let me ask you a little bit of a bigger picture question. The Alaska power plant project has been a thorn in your side for several quarters and now it looks like it will stretch into 3Q. Maybe you can just talk about some of the lessons learned from that project and how it could impact what you plan to do in moving the Company forward. And how do you limit these types of issues from coming up in the future as you try to move into an adjacent markets? And is fixed price power a business that you want to be in?

Duke Austin (President & CEO):

Good question. From my standpoint, we're going to focus on our core and look at our core businesses, what we're really good at, which is people and equipment. When we look at these adjacent markets, I think we've done a nice job over time of being able to create value for our shareholders in these markets. We do have a one-off project that's more than a thorn to me, but it feels like a stick. But we are going to get that straight up in Alaska. We feel like we've got that at the right -- we're set there. So at the right outcome and also with the customer.

What we're going to do on the electric power side is we were in solar, we were looking at that. And our customers, all of them are building some natural gas. So again, adjacent market, our customer was driving us that way. We'll make sure that we negotiate good contracts when we look at those projects and have the right management team. We have brought in a seasoned management team here at Quanta on that project, so we're comfortable with where we're at there.

Operator:

Chad Dillard.

Chad Dillard (Analyst - Deutsche Bank):

Just wanted to push you a little bit on the large transmission projects. Bookings are pretty nicely in electric power during the quarter, but could you talk a little about what you're seeing in terms of mix of large versus small projects and then compare that to what you're seeing in revenue? I want to understand what the trajectory is and how to think about the next 12 to 18 months.

Duke Austin (President & CEO):

Yes, again, whether you look at it from a large standpoint or a small standpoint in transmission, we do see both kinds of projects all the time. It's more about the capital budgets in the transmission market of our customers. And all those capital budgets continue to be robust. So whether it comes out in a big large project or one that's divided into three, the project itself and the need for transmission is still there. And we see both. We have large transmission in our backlog, such as the one in Canada. We continue to bid on projects such as the clean line Northeast clean RFP, with Eversource. That's also something that we're looking at. If that goes, it changes the way, big versus small.

But again, there will always be intermittency between big and small as we move forward. It's more about the whole capital budget and how we look at it internally. So we're focused on returning our core business in the Electric segment to the 10 to 12, with even small or large transmission.

Chad Dillard (Analyst - Deutsche Bank):

Got it. And then just moving on to Canada. What are you expecting in terms of revenues in that end market? And how are you thinking where utilization is? Do you think you need to do a little bit of restructuring there? And can you pull some of your assets over to the US to support some of the mainline build out there?

Derrick Jensen (CFO):

As it stands, I'd say that Canadian revenues are probably going to be somewhere in the 15% to 20% range. They're down a little bit as compared to what you've seen in the past. And then relative to costs and efforts there, a large portion of what we're looking at from a margin perspective is focused on the Canadian operations, and in fact, through the latter part of 2015, the largest reductions in cost have come out of Canadian markets. So we're very focused on ensuring that we'll be able to position that market to be comparable to, or complementary to, the efforts that we're taking to be able to get the margins back into the profile that Duke has spoken about.

As far as the movement of people and equipment, we do look at that regularly back and forth between Canada and the US. It's all, obviously, very economic and market dependent and often times, job dependent. So we take advantage of that to the extent that we can, when the opportunity presents itself, based upon the individual projects.

Duke Austin (President & CEO):

And I would say that geographically, there's always cycles in the market. And by no means, the projects in Canada are there. It's just about when they come online or when we start bidding them. And we can't tell yet where that's at, due to the regulatory environment there. But the demand and to move both gas and product from East to West, and also if they look at some clean energy standards, you'll see some dynamics go on with renewables there that will need transmission. It's a robust bidding environment right now in Canada. But you just can't tell when it's going to move.

Operator:

John Rogers, D.A. Davidson.

John Rogers (Analyst - D.A. Davidson & Co.):

Just a couple quick things to follow up on. Duke, in terms of the acquisition strategy at this point, you had a couple of small deals in the quarter, what's your thoughts on priorities here, especially given your look at the market? And does that include telecom out beyond 2017, or you probably don't want to talk about it at this point?

Duke Austin (President & CEO):

Yes. Our priority is to focus on our core business and to return our margins back to what we expect. As we look at, from an acquisition standpoint, we'll be strategic in how we make them. Again, we don't necessarily have a footprint today of a list of people that we're out trying to get or some certain company that we're after to acquire. It's more about finding adjacencies where we can leverage what we already have and make it much larger. And we're also looking at ways we can grow organically. It's not just about us looking at acquisitions or enhance the shareholder value, if we don't grow. So all those things come into play when we're looking at our strategy.

John Rogers (Analyst - D.A. Davidson & Co.):

Sure. But at this point, given how you look at the market, what the competitive landscape looks like, what your needs are, are there more opportunities interest in oil and gas versus transmission, or any thoughts there?

Duke Austin (President & CEO):

No, again, we try to fill a strategic area, if we make an acquisition, through adjacencies or whatever it may be. The customer is also asking us to do different things, so we look at that, as well. So all those things come into play. But I would say in general, we watch how much acquisitions we make in one part of the business versus the other. We want to make sure that we're geographically as well as service line have a lot of variability in our service offerings.

Operator:

William Bremer.

William Bremer (Analyst - Maxim Group):

First question, just give us a sense, if you can, on the amount of spreads that you'll be utilizing in the second and third quarter. First question.

Second question. We've had a lot of weather issues in certain parts of the country, even subsequent to the quarter. Maybe give us a sense on what was the impact during the quarter and what you're seeing the potential impact in the second here.

And finally, just an overall update and congrats on the announcement of the pipeline in Australia. Can you give us a little more granularity there?

Duke Austin (President & CEO):

Let me take a little bit on the pipe. We said in the prepared remarks we'd be on more projects than any time in 2010. I don't really want to get into spreads, because I think it's a loose term and I don't want to try to define that. But again, what we said is we'll be on more projects than any time besides 2010. So it will be robust in the pipeline market.

As far as again, there's some fires in Canada. I know everyone's seen that in the news. We're worried about our workforce right now and making sure everybody's safe, and they are, and our customers and make sure their employees are safe. So we reach out to them right now and try to get that. That's our first and foremost what we're after today and into the week. But I don't foresee that being an impact to us. It would be minor, if it was, in the second quarter. And I think the rest of it --

Derrick Jensen (CFO):

The third part was Australia.

Duke Austin (President & CEO):

Australia, we did pick up a line in Australia, a condensate line. And so we're happy with that and our guys in Australia are executing on that, as we speak.

Derrick Jensen (CFO):

Bill, I'll add a little bit from the second quarter. We do have, as Duke mentioned earlier, Canadian breakup to deal with. And so that will -- and probably see a little bit lower margins than Electric Power side from first quarter to second quarter. But more broadly, and to the other weather impact, it's too soon to say as to how the aggregate projects move, but we will be mindful of the weather relative to the overall margin expectation.

Operator:

Jeff Volshteyn.

Jeff Volshteyn (Analyst - JPMorgan):

When you look at your recent projects that you won in the first quarter, can you share some color on where they are located? Are they all mainline? How far along are they in their regulatory processes?

Duke Austin (President & CEO):

Yes, in general, when we're talking about projects in guidance, we take into account most of the regulatory issues. So those have been taken into account. As far as where they're at, we're not going to get into the details of the projects at this point, other than to say that we think we'll be executing on them and we'll be on more mainline then we have since 2010. And we'll continue to say that. So that's kind of where we're at on it.

Jeff Volshteyn (Analyst - JPMorgan):

Okay. And as a follow-up, just to clarify. So for 2016, I understand you don't have any uncommitted projects to get to the midpoint of your guidance. But how much of your 2016 revenues have you already won and have in he backlog and under contract versus how much you still have to win to get to that midpoint?

Derrick Jensen (CFO):

First, a clarification that we have no uncommitted large pipeline projects. We do have uncommitted work in the Oil and Gas segment associated with the remaining portions of the business, the distribution work, integrity, things like that. But then to that end, if we have no uncommitted, that means that everything is currently in backlog that we would anticipate to execute on relative to the midpoint of our guidance on that large diameter pipe.

Operator:

Thank you. This does conclude our Q&A session today. I'd like to turn the call back to our management team for any closing remarks.

Duke Austin (President & CEO):

I would like to thank you all for participating in our first quarter 2016 conference call. I also want to thank my family for supporting me in the role and the guys that are with us on a daily basis out executing work. Thank you.

Thank you for your interest in Quanta Services , and this concludes our call.

Operator:

This does conclude today's program.