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LIME - Q3 2015 Lime Energy Co Earnings Call

EVENT DATE/TIME: NOVEMBER 12, 2015 / 9:30PM GMT



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Mary Colleen Brennan *Lime Energy - CFO, Treasurer*

CONFERENCE CALL PARTICIPANTS

Glen Akselrod *Bristol Capital Ltd - Analyst*

John Ford - *Private Investor*

PRESENTATION

Operator

Good day, ladies and gentlemen and welcome to Lime Energy 2015 Third Quarter Conference Call. At this time, all participants are in a listen-only mode. Later we will conduct a question-and-answer session and instructions will follow at that time.

(Operator Instructions).

And as a reminder, this conference call is being recorded. I would now like to turn the conference over to Glen Akselrod, Spokesperson. You may begin.

Glen Akselrod - *Bristol Capital Ltd - Analyst*

Thank you Victoria and good afternoon and thank you everyone for taking the time to join Lime Energy's 2015 third quarter results conference call. With us today is Adam Procell, President and CEO and Colleen Brennan, company's CFO.

Before I hand the discussion over to Adam, I want to remind everyone that the call today will include some statements that will be considered forward-looking regarding the Company's strategy, operations, and financial performance. Those statements are subject to many uncertainties in the Company's operations and business environment, some of which we will talk about in the call today.

I also refer you to the complete forward-looking statement disclosure in the earnings release, which is incorporated by reference for the purposes of this call. And I also would like to refer you to the disclosures made in the Company's quarterly and annual filings with the SEC. Finally, before we get started, I want to mention this call is being broadcast live over the Internet and can be accessed on the Thomson Reuters network. There will be a transcript posted on the Lime Energy website once available after the call.

With that, I will hand the discussion over to Adam.

Adam Procell - *Lime Energy - President, CEO*

Thank you, Glen. And I want to thank everyone for getting on the call. I want to thank first of all our clients who we work with hand in hand everyday and for their continued partnership for collaborating with us on innovative approaches to delivering energy efficiency in what is a very dynamic time in the utility industry. I want to thank all of our Lime Energy team members for their continued hard work and in building something very special and what we have accomplished in the last year is remarkable and few people would have believed that it was possible. But the men and women that make up our team believed it and so today I am going to cover some of these accomplishments and high-level overview of the numbers.

As always which Colleen will then get into great detail on. I am also going to talk to you today about why I'm excited to come to Lime Energy every day. One year ago Lime Energy had significant negative working capital which threatened our ability to continue to operate and we were working



hard to find a significant new investor that would help us stabilize our financials. We were trying to repeat a \$52 million revenue and go from a year of significant losses in 2013 to breakeven in 2014. That was when we met one year ago.

But even at that time we talked about a plan for significant growth, we talked about acquisitions, talked about the development of innovative new products and services. We talked about being a profitable \$100 million plus company in 2015, a year that at that time was just seven weeks away. No doubt there were skeptics but the Lime Energy team believed in these goals and we've walked the path together. We've walked the path through two major capital raises, through the acquisition and integration of our major competitor, through winning several major utility program contracts, and integrating the operation of these two companies. And today we can report that we're on track with our objectives.

First on the financial performance, Colleen again, will speak in greater detail to our year-to-date 2015 financial performance, but on the most critical metric for a public company, the year-over-year progress is impressive. Our Q3 revenue of \$32.2 million represents a 106% year-over-year growth. Our Q3 gross profit is up a 127% with gross profit margin of 34.3% up from 31.1% a year ago.

In the third quarter our SG&A grew by 91%, which is almost 30% slower growth than the gross profit growth. All of this resulted in \$2.2 million of adjusted EBITDA in Q3 excluding certain onetime costs. For the nine months ended September 30, we see the same scenario play out. Growth near the 100% mark with gross profits increasing out - with the increases in gross profits outpacing SG&A increases by nearly 30%. The result on a year-to-date basis through nine months is \$4.4 million of adjusted EBITDA, again excluding certain one-time costs.

So in just one year we've become the Company that we talked about last November. Through a combination of belief, determination, hard work and good strategy, we've done what didn't seem possible. We're always happy to meet our objectives but we're never satisfied that we've accomplished all that we can.

So let me talk to you now about the future of Lime Energy and why I'm so excited to come to work at Lime every day. Good people working at a great company that is doing important things. That's the reason. The things that Lime Energy does are important. How important? How about helping American businesses to improve performance by upgrading facilities while lowering energy cost. Helping utilities to reduce emissions from power production and comply with environmental mandates. Helping the country to increase our energy productivity, making ourselves more competitive globally; training workers in new green jobs as the nation shifts to a low carbon economy.

Climate change mitigation is in fact very important to the United States and Lime Energy is at the forefront of delivering real results to this problem. Delivering energy-efficient carbon-reducing facility upgrades in the low and moderate income communities is particularly important. So much so that the most comprehensive environmental regulation of our time, the EPA's Clean Power Plant is offering double credit for clean energy solutions which benefit these communities during the first few years of compliance under the plan.

Lime Energy has built a business that is leading the way in energy-efficiency deployment in low and moderate income communities. We implement facility upgrades for thousands of small businesses in these communities every year, and we recently joined a White House initiative by pledging to do 1,000 more of these projects. Great company, Lime Energy is a great company.

The way to run a great company is to attract the best people that would make great strides in making this a company that anyone would want to work for. Initiatives around employee engagement, training, community involvement, improvements in benefits from instituting a 401-(k) match to increasing company contributions to health insurance and improving our health insurance provider. Managing with an open-door policy, where politics are minimized and the voices of all employees are heard.

We've made slow and steady progress on this front and we will continue to work to ensure that Lime Energy is a great place to work. There are many adjectives that could be used to describe Lime Team members, but what is relevant is that we are good people. Our people are led by an overarching commitment to our most important tenet which is integrity. The people that we want at Lime Energy are those who are passionate about the work that the Company does, who believe in the goals of the Company, and who respect one another and value everyone's contributions. So I am excited everyday when I come to work because I am joining good people at a great company that is doing important things.



Finally, during the third quarter we moved our headquarters to New Jersey and we signed a lease for new headquarter space in Newark. As the Company committed to urban revitalization and sustainable cities, we are able to walk the walk by bringing our operational hub to the brick city where we were able and fortunate enough to celebrate last month along with the dignitaries representing the Mayor of Newark, the Governor of New Jersey, and Senator Cory Booker at a ribbon cutting which marked our commitment to the State of New Jersey and to the city of Newark. With that I will turn it over to Colleen to go over the financials in more detail.

Mary Colleen Brennan - *Lime Energy - CFO, Treasurer*

Thanks Adam. Good afternoon everyone and thanks for joining us again. I am going to start here with a brief overview of the results for the three and nine months periods ended September 30, 2015. Beginning with the results of the quarter; our consolidated revenue increased 106.4% or \$16.6 million to \$32.2 million during the most recent quarter as compared to \$15.6 million for the prior year period. This was primarily driven by the acquisition of EnerPath and by higher revenue from our existing utility programs. We expect revenue from our energy efficiency business to continue to show substantial growth for the fourth quarter over the same period in 2014.

Our gross profit for the quarter increased 127.5% or \$6.2 million to \$11 million from \$4.8 million from the prior year period. Our gross profit margin improved from 31.1% during the third quarter of 2014 to 34.3% during the third quarter of 2015. The improvement in our gross margin was the result of improved efficiencies in existing programs and higher margin contributions from our new programs, including the EnerPath programs and some renewed programs. We expect our gross margins for the fourth quarter to remain in the same range with possible fluctuations up or down depending on the level of contribution from individual programs.

Our selling, general, and administrative expenses increased \$4.5 million from \$4.9 million during the third quarter of 2014 to \$9.4 million during the third quarter of 2015. With the acquisition of EnerPath, our combined SG&A expense as a percentage of revenue declined to 29.1% for the third quarter of 2015 as compared to 31.4% for the same period of 2014.

Our costs related to the restatement we completed in July of 2013 and the associated stockholder lawsuits and SEC investigations totals \$65,000 during the third quarter of 2015, which was \$29,000 less than the \$94,000 we incurred during the third quarter of 2014. For the balance of 2015 we expect our cost-cutting initiatives and successful integration of the EnerPath acquisition will continue to contribute to reductions in our SG&A expenses as a percentage of revenue relative to last year.

During the third quarter of 2015, we incurred acquisition and integration cost of \$529,000 related to the acquisition of EnerPath. Amortization of intangibles resulted in cost of \$285,000 during the quarter. We also incurred \$246,000 of interest expense related to financing for the EnerPath acquisition offset by a gain of 1.3 million from a change in the derivative liability.

The Bison note which we issued for financing EnerPath acquisition included a conversion feature that is required to be bifurcated and recorded as a derivative liability. The derivative liability is recorded as fair value which was determined to be 7.7 million and 6.4 million as of June 30, 2015 and September 30, 2015 respectively. This change in value of the derivative liability, which has an inverse relationship to the movement in our stock price was recorded as the gain. We did not incur any of these costs in the third quarter of 2014.

The increase in our quarterly revenue in combination with the improvement in our gross margin and reduction in our SG&A expense coupled with the gain from the change in derivative liability contributed to income from continuing operations of 1.9 million for the last quarter versus a loss of \$45,000 for the third quarter of 2014.

There was a loss from discontinued operations of \$46,000 compared to a gain of \$136,000 in the prior year period. We have one legacy public sector project that we are working to close out, that is the only ongoing activity related to business we have either sold or closed down. Until this project is completed we expect we'll have small quarterly losses from discontinued operations.

All of this contributed to net income of \$1.8 million for the quarter compared to \$91,000 for the prior year period. Adjusted EBITDA increased \$1.4 million or 754.3% to \$1.6 million from \$86,000. When excluding acquisition cost, expenses related to the restatement caused them to send the stockholder lawsuits and costs and expenses related to the SEC investigation, adjusted EBITDA increased \$1.7 million or 343.7% to \$2.2 million.

We report our financial results in accordance with generally accepted accounting principles. However, from time-to-time we used certain non-GAAP financial measures in evaluating and discussing the Company's results and performance. We believe these non-GAAP measures supplement the understanding of our financial performance by providing additional information to evaluate our operating performance using criteria used by our management in evaluating our performance in comparison to prior results.

One such measure is adjusted EBITDA which excludes certain financial information compared with net income or loss, the most directly comparable GAAP financial measure. A reconciliation of non-GAAP financial measures discussed during the call with the most comparable GAAP measures is available in the Company's earnings announcement released today as well as on the Investor Relations section of the Company website at www.limeenergy.com/investors.

Now turning to the nine month results, a consolidated revenue for the nine months period ended September 30, 2015 increased \$41 million or 98.8% to \$82.4 million due to the reasons outlined earlier. All the programs are running at steady state levels, therefore we expect our growth in future periods to continue to moderate unless there is an increase or decrease in the number of programs on which we are working.

Our gross profit for the first nine months of 2015 increased a 110.9% or \$14.4 million to \$27.4 million. Again, this increase was driven by the acquisition of EnerPath as well as higher revenue and improved margins from our utility business. Our consolidated gross profit margin improved from 31.3% to 33.3% year-over-year and we expect it will improve slightly in this quarter. Our SG&A expense increased by \$10.1 million or 69.9% to \$24.6 million during the first nine months of 2015 compared to the \$14.5 million of expense for the first nine months of 2014.

The Company's acquisition of EnerPath resulted in costs of \$1.5 million during the first nine months of 2015. Amortization of intangibles resulted in costs of \$594,000 during the first nine months of 2015. We also incurred \$645,000 of interest expense, \$1.4 million extinguishment of debt, and \$814,000 loss from the change in the derivative liability in connection with the financing for the EnerPath acquisition. As stated earlier the derivative liabilities recorded at fair value which was determined to be \$5.6 million as of the note issuance date and \$6.4 million September 30, 2015.

The \$814,000 increase in the fair value of the derivative liability was recorded as a loss. We did not incur any of these costs in the first nine months of 2014. SG&A costs related to our restatement and stockholder losses totaled \$287,000 for the first nine months of this year compared to \$690,000 for the comparable period of 2014. With the acquisition of EnerPath, our combined SG&A expense as a percentage of revenue declined to 29.8% for the first nine months of 2015, as compared to 34.9% for the same period of 2014.

However when adjusted for onetime expenses related to the restatement and the stockholder lawsuits and the SEC investigation, SG&A declined to 29% of revenue.

Our loss from continuing operations decreased \$432,000 or 30% to \$1 million for the first nine months of 2015 from a loss of \$1.4 million for the same period in 2014. Adjusting for the onetime restatement and legal expenses of \$287,000, our loss from continuing operations decreased \$29,000 or 3.8% to \$719,000 from \$748,000 in the prior year period. We are very focused on continuing to increase the profitability of the energy efficiency business, primarily through increases in revenue, while continuing to control the growth of our overhead cost.

Adjusted EBITDA increased \$1.9 million or 278.7% to \$1.2 million from a loss of \$686,000. When excluding acquisition cost, expenses related to the restatement, cost of the defense, and the stockholder lawsuits, cost and expenses related to the SEC investigation, and loss on the extinguishment of debt, adjusted EBITDA increased \$4.5 million or 935.2% to \$4.4 million from a loss of \$91,000.

In terms of liquidity, we had \$8.1 million of cash and cash equivalents, including \$1.3 million of restricted cash as of September 30, 2015 compared to \$6 million, including restricted cash of \$500,000 as of December 31, 2014. Net cash used in operating activities generated \$2 million during the first nine months of 2015 compared to consuming \$8.2 million during the year earlier period, representing an increase in cash of \$10.2 million of the prior year period.

The cash generated by operating activities before changes in assets and liabilities, which is basically our net loss excluding non-cash items, increased by \$1.2 million to \$1.4 million, up from the \$220,000 generated during the third quarter of 2014. The changes in assets and liabilities, i.e., the change in net working capital generated \$573,000 during the first nine of 2015 compared to consuming \$8.4 million during the prior year period.

We expect to generate or consume more modest amounts of cash which changes the working capital related to assets and liabilities in future periods if our sales grow as we anticipate they will. We consumed \$11.9 million of cash in investing activities during the first half of 2015 compared to \$443,000 during the first nine months of 2014. The cash consumed during the first nine months of 2015 included the \$11 million used to acquire EnerPath and \$777,000 used for capital expenditures. \$466,000 of which was used to continue to develop software platforms used by our utility programs. All of the cash consumed during the first nine months of 2014 was for capital expenditures, the largest portion of which was used to continue to develop the software platform.

During the first nine months of 2015, financing activities generated \$11.3 million of cash compared to \$3 million generated during the first nine months of 2014.

Approximately \$11.7 million related from the issuance of the Bison note in the first quarter of this year was partially offset by \$480,000 of cash paid for deferred financing costs.

During the nine months period ended September 30, 2014, we raised \$2 million due to the sale of shares of Series B preferred stock, and \$1 million from the issuance of the 2014 notes. This was partially offset by \$11,000 of costs related to the preferred stock issuance. On July 24, 2015 we entered into a loan and security agreement with Heritage Bank of Commerce. The loan agreement provides us with a secured key revolving credit facility -- for which we are permitted to borrow up to an aggregate of \$6 million which is available to fund working capital and other general corporate purposes. Our ability to draw on the credit facility is subject to customary conditions.

As of September 30, 2015 there were no borrowings against the credit line. We continue to closely monitor our working capital position and believe that if the profitability of our core business, the energy efficiency business, continues to improve as we believe it will, our operations should remain cash flow positive. I think that covers everything for the third quarter. So, now I will turn it back over to Adam.

Adam Procell - Lime Energy - President, CEO

Thank you, Colleen. In closing Lime Energy finds itself at the confluence of several disruptive changes, from the role of the utility to environmental regulations, to lighting and communications technology, to energy efficiency project financing. We believe that we have had the right strategy since the inception of our utility solutions business in 2009 and that that this strategy has given us an advantage in the market. We remain focused on being innovative which we believe is core to accomplishing our goal of being a sustainably profitable company.

Before we open it up for questions, I want to reiterate that Lime Energy is projecting profitability for the full year 2015 with revenue that we are confident will exceed \$100 million. With that we will open it up to questions.

QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions). We have a question from John Ford, a private investor. Your line is open.

John Ford - - Private Investor

Hi guys, good work, EPS positive. I have a question related to that. So 2015 as a whole will be profitable, so far you're not because you have minus \$0.37 and now correct me if these numbers are not right, but you have roughly a \$0.37 loss for Q1 and Q2, a plus \$0.05 for Q3 which means we need to earn at least \$0.32 in Q4 just to breakeven so that your full year 2015 profitability comes through, you need to earn more than \$0.32 in Q4. Tell me where I'm wrong in that or if I'm not.



Adam Procell - Lime Energy - President, CEO

John, we going back, thank you for the question, well, so going back to what Colleen was talking about regarding adjusted EBITDA onetime costs, I think we've talked in the past about this being a year where we have a lot of those costs. And so I think that when we talk about earnings per share positive I think that, that would be - it's going to be a stretch for us to hit that on full year. So you bring up a good point on the earnings per share. I think when you talk about adjusted EBITDA positive for the full year, given the accounting anomalies in this year that Colleen talked about.

John Ford - - Private Investor

Okay. So it's EBITDA positive not GAAP positive?

Mary Colleen Brennan - Lime Energy - CFO, Treasurer

Correct.

John Ford - - Private Investor

Okay. Alright, that makes sense. And then revenue was flat from Q2 to Q3, is that expected to continue flat but decreasing costs?

Adam Procell - Lime Energy - President, CEO

Yes, we are anticipating a fourth quarter at the top line that resembles the third quarter.

John Ford - - Private Investor

Okay. Alright, and then when do you expect the onetime costs, even though they are minimal, to pretty much be gone?

Adam Procell - Lime Energy - President, CEO

There's a few categories of those. I'll let Colleen chime on this, she keeps close track of those. There are a few - I will just mention that there are a few categories of those. Some of those have to do with acquisition activity, which is something that we would reasonably anticipate continuing in the future. Those the costs that have to do with the SEC investigations, shareholder lawsuits, have already dropped off quite a bit. So I'll let Colleen may be clarify that a little bit.

Mary Colleen Brennan - Lime Energy - CFO, Treasurer

Yes. That's the case. The shareholders' lawsuits, all the costs related to those are gone. We still have some minimal costs for the SEC because that investigation is ongoing. So we will have some legal expenses continuing for that may be another month or so, I would guess. And as for the, some of the one - what we consider onetime costs, some of the integration costs, we're still really integrating the acquisition of EnerPath. So some of those costs probably will continue maybe for another couple of months, quarter, yes, may be through Q1 of 2016.

John Ford - - Private Investor

Okay, alright. I've got a couple of more questions but I'll drop out and let somebody else in and I'll come back later. Thanks.



Adam Procell - Lime Energy - President, CEO

Thanks, again, John.

Operator

(Operator Instructions). And we have a follow up question from John Ford. Your line is open.

John Ford - - Private Investor

Okay. This just has to do with your legacy business versus your EnerPath division or where do you expect the bulk of your profits to come from or are they pretty much split up, split in half?

Adam Procell - Lime Energy - President, CEO

So, it's an interesting question. So they - when we acquired that company the revenue comes from complimentary programs, right? So we have seven programs, they have five, now together we have 12. The gross profit from the EnerPath programs and Lime programs tends to be very closely related. So there's the there's a very similar amount of gross profit being generated by legacy Lime programs and legacy EnerPath programs.

What happens when you go to the next level is that we have integrated all of the corporate services really from day one in March so, it is kind of hard from a financial standpoint to say where those profitability is coming from and we think that we are going to be able to demonstrate leverage in 2016 across some of those corporate costs. But the profitability, they run very similar programs that are similarly profitable to the ones that Lime Energy was running.

John Ford - - Private Investor

Okay, my last question just has to do with the EPS, so your nickel EPS this quarter I would assume is similar to next quarter or is there anything drastic or that will reduce cost to make that number bigger and that is my last, last question is and when do you expect EPS positive to begin, or you are giving guidance on that?

Mary Colleen Brennan - Lime Energy - CFO, Treasurer

Not giving guidance on that at this point. But I would imagine that it is going to be fairly flat in Q4 for the earnings per share as compared to where they are now.

John Ford - - Private Investor

Okay, and how would we project that going forward in 2016, I mean is there anything seasonally or otherwise that would make that number go up or down?

Adam Procell - Lime Energy - President, CEO

Do you mean in particularly the earnings number or are you talking about from a revenue standpoint.



John Ford - - *Private Investor*

In particularly the earnings number?

Adam Procell - *Lime Energy - President, CEO*

No, I don't think that there is anything that would make that seasonal. We think that the double track was with our revenue which has flattened out quite a bit from what we have had in the past. It always tended to be slower in the beginning of the year and we don't really see that. Now we do grow when we project growth we are for example starting up a new program or winning a new contract that revenue maybe further back in a year or when they gear up for that growth from an SG&A standpoint prior to the revenue. So we do have some of that effect so, I would say that as we continue to grow there would be probably some seasonality to the earnings per share if anything it would be that it would -- it would be lower earlier in the year than it would be later in the later quarters.

John Ford - - *Private Investor*

Okay, alright that's it for my questions. I appreciate the time guys. And good job on turning EPS positive. That is a big deal.

Mary Colleen Brennan - *Lime Energy - CFO, Treasurer*

Thank you.

Adam Procell - *Lime Energy - President, CEO*

Thanks very much John.

John Ford - - *Private Investor*

Thank you.

Operator

Thank you. And I am not showing any further questions in queue at this time. I would like to turn the call back over for any closing remarks.

Adam Procell - *Lime Energy - President, CEO*

Thank you Victoria and again just thank everybody for being on the call. Reiterate the thanks to our clients, our partners, and all the team members here at Lime and we are very excited about how far we have come in a year and more excited about where we are going. So, look forward to talking to everybody again in the New Year.

Operator

Thank you. Ladies and gentlemen this concludes today's conference. You may now disconnect. Good-day.



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