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APi Group Corp. (APG)

Q1 2021 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning, ladies and gentlemen, and welcome to APi Group's First Quarter 2021 Financial Results Conference Call. All participants are now in a listen-only mode until the question-and-answer session. Please note this call is being recorded. I will be standing by should you need any assistance.

I'll now turn the call over to Olivia Walton, Vice President of Investor Relations at APi Group. Please go ahead.

Olivia Walton
Vice President-Investor Relations, APi Group Corp.

Thank you. Good morning, everyone; and thank you for joining our first quarter 2021 earnings conference call. Joining me on the call today are Sir Martin Franklin and Jim Lillie, our Board Co-Chairs; Russ Becker, our President and CEO; and Tom Lydon, our Chief Financial Officer.

Before we begin, I would like to remind you that certain statements in the company's earnings press release announcement, and on this call, are forward-looking statements, which are based on expectations, intentions and projections regarding the company's future performance, anticipated events or trends and other matters that are not historical facts.

These statements are not a guarantee of future performance and are subject to known and unknown risks, uncertainties and other factors that could cause the actual results to differ materially from those expressed or implied by such forward-looking statements. In our press release and filings with the SEC, we detail material risks

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that may cause our future results to differ from our expectations. Our statements are as of today, May 12, and we have no obligation to update any forward-looking statement we may make.

As a reminder, we have posted a presentation detailing our first quarter financial performance on the Investor Relations page of our website. Our comments today will also include non-GAAP financial measures and other key operating metrics. The reconciliation of, and other information regarding these items, can be found in our press release and on our presentation.

Before turning the call over to Martin, I would like to thank everyone that participated in our first ever investor event on April 22. A replay of the webcast is available along with the presentation slides on the Investor Relations page of our website.

It is now my pleasure to turn the call over to Martin.

Martin E. Franklin

Co-Chair, APi Group Corp.

Thank you, Olivia. Having just passed the one year anniversary of our listing on the New York Stock Exchange, I'm proud of what we've accomplished so far as a public company. And I'm pleased to say that our original investment thesis that I reviewed with all you at our investor event has proved to be progressing as well as we could possibly have hoped.

Our first quarter results speak to the strength of the company's recurring revenue services-focused business model, which drives enhanced margins. We're excited about the organic prospects for the business and also believe there are significant opportunities to accelerate growth, service offerings and margin expansion through continued strategic M&A.

As many of you know, we have always maintained a disciplined approach when it comes to M&A. That will continue to be the case here and we will remain focused on opportunities that will be accretive, not just to the financial profile of the company, but also to the cultural story of APi and its commitment to leadership development. This is a hugely fragmented market space and we are very well positioned to pursue a fertile selection of acquisition prospects.

With that, I'll turn the call over to Russ.

Russell A. Becker

Chief Executive Officer, President & Director, APi Group Corp.

Thank you, Martin; and good morning, everyone. Thank you for taking the time to joining our call this morning. I would also like to thank you again to those who participated in our first ever investor event a few weeks ago. We are pleased to deliver our first quarter results with net revenues slightly above and margins in line with our previously communicated guidance.

As you've heard me say on prior calls, the health and well-being of each of our employees and the communities in which we serve, remain our number one priority. This focus and other foundational priorities provides the platform from which we can continue to enhance shareholder value. During today's call, I will provide a summary of our first quarter results, the outlook including key growth drivers and margin expansion opportunities, an update on strategic M&A efforts, before I turn the call over to Tom. Tom will walk you through our most recent results and guidance in more detail.

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Before I walk through the highlights from our first quarter results, I would like to remind everyone that APi did not begin to experience negative impacts from COVID-19 until mid- to late-March last year. Therefore, we are comping this Q1 against the Q1 largely free from COVID-19 last year. Also, as a reminder, our business ramps up as we move through the calendar. Our revenue is typically lowest at the beginning of the year and during the winter months, because cold, snowy or wet conditions can cause delays with our work, particularly in our Specialty and Industrial Services segments, where a majority of the activity is performed outdoors. As the weather improves, so do our opportunities.

During the first quarter of 2021, we experienced extreme weather conditions at several of our businesses, which tends to put pressure on margins. Therefore, we also have a relatively tough margin comparison driven by unfavorable year-over-year weather in certain markets we serve. All of that being said, I'm very pleased with our performance and execution in the first quarter. Key highlights from our performance for the three months ended March 31, 2021, compared to the prior-year period include the following.

Number one, net revenues increased on an organic basis by 2.4% compared to the prior-year period. This excludes the anticipated decline in Industrial Services. Growth was driven by increased demand and timing of projects in our Safety and Specialty Services segments, offset by project delays in job site disruptions due to continued negative impacts of COVID-19 and unfavorable weather conditions. Second, continued focus in our ongoing goal of growing recurring inspection and service revenue, which we believe helps build a more protective moat around the business.

Third, adjusted gross margins grew to 23% which is an increase of 72 basis points. This is due to the improved mix in Safety Services and disciplined project and customer selection in Specialty Services. Fourth, an adjusted EBITDA margin expansion of approximately 20 basis points, driven primarily by the factors I mentioned as drivers of gross margin expansion. I'm inspired and appreciative of the resiliency and commitment of our approximately 13,000 team members who remain focused on serving customers despite the headwinds, both literally and figuratively, that they were facing this quarter. I'd like to thank them for their continued efforts. Their ongoing leadership efforts continues to demonstrate that our leaders are a competitive advantage and help drive shareholder value.

Before turning the call over to Tom, I'd like to spend a few minutes discussing our outlook and opportunities within key end markets, followed by a summary of margin expansion opportunities to drive further value creation including strategic M&A. We believe that our revenue diversification across geographies, end markets, customers and projects provides us with stable cash flows and a platform for organic growth.

The average size of our projects including all three of our segments is less than $100,000, which helps our ability to pass on raw material costs on a timely basis. Our average project duration is relatively short, so we don't have the inflationary exposure to cost of goods sold or changes in labor expense that some of our peers may experience in an inflationary environment. On contracts that are longer term in nature, such as our multiyear master service agreements, price escalators are typically built into initial proposals.

In telecom and utilities, our largest end-market representing approximately 25% of our total consolidated net revenues, we continued to maintain strong direct customer relationships, and are focused on growing service revenue through multiyear master service agreements. We believe we are well-positioned to benefit from recently announced increases in capital expenditure guidance relating to the rollout of 5G with two of our national telecom customers. While these represent additional potential tailwinds, as you know, we have low customer concentration; and typically no customer represents more than 5% of our annual net revenues in any given year.

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As I said at our investor event, while we do not have anything built into our budget for an infrastructure bill, or stimulus that would incentivize investment in their renovation of existing infrastructure, there are certainly aspects of our business such as 5G fiber, renewable energy, potable water services, natural gas services, that would benefit from the passage of such legislation, due to our existing core competencies combined with incremental opportunities.

We also continue to see strength in the end-markets such as fulfillment and distribution centers, healthcare, high-tech. These combined represent approximately 20% of our total consolidated net revenues. The work in these end markets is more complex and we are typically awarded work based on the level of service we provide for customers as opposed to price. During our recent investor event, we provided an illustrative bridge of the drivers to reach our adjusted EBITDA margin expansion goal of 12% plus by 2023.

As many of you have heard us say before, these are all singles and doubles. If any of these initiatives fall short, we believe there are many other initiatives behind it to help propel growth and margin expansion. As we continue to focus on improving our mix, disciplined project and customer selection, pricing opportunities, leveraging our spend, driving operational excellence and realizing synergies from future acquisitions, we are confident in establishing a new recently announced goal of 13% plus adjusted EBITDA margin by year-end 2025.

We believe that strategic M&A is an opportunity to accelerate the timetable to achieve our margin expansion objectives. We continue to build our global pipeline of opportunities to grow our family of market-leading service providers. Our powered by APi structure provides us with the ability to leverage our scale, while also remaining entrepreneurial, nimble and opportunistic at the local level with reduced bureaucracy and overhead burden.

As I mentioned at our investor event, we are reviewing approximately 15 potential traditional APi M&A opportunities with revenues up to $100 million, while also partnering with Martin and Jim to look at several larger opportunities with revenues ranging from [ph] low-100s (00:11:36) up to $1 billion. We look forward to closing on some of these opportunities as we move through the balance of the year and look forward to updating you on our expected progress.

I would now like to hand the call over to Tom, to discuss our financial results in more detail. Tom?

Thomas J. Lydon

Chief Financial Officer, APi Group Corp.

Thanks, Russ; and good morning. I will start by reviewing our consolidated financial results and segment level performance, as well as our strong balance sheet and liquidity. As Russ mentioned earlier in the call, net revenues excluding Industrial Services increased on an organic basis by 2.4% compared to the prior-year period. Adjusted net revenues declined by 2.1% or $17 million to $803 million compared to $820 million in the prior-year period, primarily driven by the anticipated decline in Industrial Services.

Adjusted gross margins for the three months ended March 31, 2021, was 23%, representing a 72 basis point increase compared to the prior year. The increase was primarily due to improved mix and disciplined project and customer selection, offset by project delays and unfavorable job site conditions. Adjusted EBITDA margin for the three months ended March 31. 2021, was 7.6%, representing an approximately 20 basis point increase compared to the prior year due to the factors mentioned previously.

We continue to focus on driving strong free cash flow, and our balance sheet and liquidity profile remains strong. For the three months ended March 31, 2021, adjusted free cash flow was $23 million, representing a $30 million

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decrease compared to prior year of $53 million and our adjusted free cash flow conversion rate was approximately 38%. The expected decline in cash flow was primarily due to lower outstanding accounts receivable balances as we enter 2021 compared to 2020, resulting from lower revenue, higher compensation and benefit payments and higher capital expenditures.

As we have discussed, as revenue rebounds post COVID-19, we expect to use cash to fund working capital to drive increased service revenue and higher margins leading to increased shareholder value. As I mentioned at our recent investor event, we expect 2021 to be somewhat of a hybrid year since we are still dealing with the impacts of COVID-19. As of March 31, 2021, we had $972 million of total liquidity, comprised of $745 million in cash and cash equivalents and $227 million of available borrowings under our revolving credit facility. We had approximately $1.4 billion of gross debt outstanding, and our net debt to adjusted EBITDA ratio calculated in accordance with our credit facility was 1.75 times.

I'll now discuss our results in more detail for each of our three segments, beginning with Safety Services. Safety Services' net revenues for the three months ended March 31, 2021 increased on an organic basis by 1.5%, primarily due to increased demand and timing for HVAC services offset by continued negative impacts of COVID-19. Adjusted gross margins for the three months ended March 31, 2021, was 31.5%, representing 112 basis point increase compared to the prior year due to improved mix of work towards inspection and service revenue, combined with disciplined project and customer selection. Adjusted EBITDA margin for the three months ended March 31, 2021, was 13.5%, representing 102 basis point increase compared to the prior year due to the factors I mentioned as drivers for the gross margin expansion.

Specialty Services. Specialty Services' net revenues for the three months ended March 31, 2021, increased on an organic basis by 7%, primarily due to increased demand for the timing of our fabrication and specialty contracting services, offset by project deferrals and job site disruptions, driven by unfavorable weather conditions. Adjusted gross margins for the three months ended March 31, 2021, was 12.8%, which was relatively consistent with prior-year period, as leverage from higher volumes was offset by lower productivity due to unfavorable weather conditions. Adjusted EBITDA margin for the three months ended March 31, 2021 was 6.9%, representing an 85 basis point increase compared to the prior year, primarily due to leveraging overhead expenses with higher revenue and disciplined cost management.

Industrial Services. In Industrial Services, net revenues for the three months ended March 31, 2021, declined as expected due to decreased volumes, primarily driven by our strategic focus in improving margins as opposed to growing top line. As Russ detailed in our investor event, we remain focused on growing the integrity side of pipeline transmission which is statutorily driven, as transmission companies are required by law to maintain their existing pipeline systems to ensure they are safe. Adjusted gross margins and adjusted EBITDA margin for the three months ended March 31, 2021, was negative 12% and negative 24% respectively, compared to 16.2% and 10.1% respectively in the prior-year period. The decline was primarily driven by unabsorbed costs for leases and equipment due to lower volume.

2021 guidance. As we confirmed during our recent investor event, our full year guidance for 2021 remains unchanged. We expect adjusted net revenues for 2021 to range between $3.65 billion and $3.75 billion, as we focus on driving inspection and service revenue combined with our disciplined approach to project and customer selection. We expect adjusted EBITDA for 2021 to range between $405 million and $419 million. We expect capital expenditures to be approximately $55 million, and normalized appreciation approximately $60 million.

Our cost of capital is approximately 5%, and our adjusted mid- and long-term effective tax rate remains approximately 21%. And our estimated fully adjusted diluted share count is approximately 205 million. As we look

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at our guidance for the second quarter, and as we said earlier this year, we expect adjusted net revenues to range from $925 million to $950 million with adjusted EBITDA margin between 11.4% and 12.1%

Before turning the call over to Jim, I wanted to advise everyone that we plan to file two S-3 registration statements later today. The first S-3 completes our previously disclosed registration rights commitment to Viking Global, and the second represents a universal shelf registration. While we have no immediate plans to raise public equity or debt, we believe it is prudent to have the flexibility to access the capital markets on a timely and efficient basis as or when needed.

When declared effective by the SEC, the universal shelf will allow the company flexibility from time to time to offer to sell up to $500 million of public equity or debt. Both filings are purely administrative undertakings and are not meant to foreshadow any known or anticipated activity.

I will now turn the call over to Jim.

James E. Lillie

Co-Chair, APi Group Corp.

Thanks, Tom. Good morning, everybody. We are pleased with our first quarter results, despite having a tough comparison relative to the first quarter in 2020 due to COVID-19 and the unfavorable weather conditions, as Russ mentioned. We are also very pleased that the team continues to execute against our long-term strategic plans. I believe that those of you who joined us for our Investor Day saw depth to our leadership bench and gained additional insight into the various opportunities we have to drive earnings and margin expansion, which we believe should drive multiple expansion.

With one full year as a New York Stock Exchange-listed public company now behind us, we are proud of the track record of strong results we've accomplished in an unprecedented and challenging macroeconomic environment. The strong performance speaks to the leadership team, the strength of our business, our protective moat around the business, driven by recurring revenue and our financial discipline as we continue to focus on shareholder value creation.

We believe that in addition to our strong organic revenue growth prospects and margin expansion opportunities, we also have significant M&A opportunities in a highly fragmented industries. Our conservative balance sheet and liquidity profile provide us with ample capacity to absorb additional accretive acquisitions. As Tom mentioned, we ended the quarter with nearly $715 million of cash and a net debt to adjusted EBITDA ratio of 1.75 times, which is below our targeted long-term net ratio of 2 times to 2.5 times.

As we said before, our priority for our use of cash is to explore opportunistic acquisitions as we move through the rest of the year. We're excited about potential targets in areas where we can leverage our existing competencies and infrastructure such as fire and life safety, while also evaluating opportunities to expand our menu of service offerings in the areas such as elevator and escalator services. We believe there is value in being a one stop shop solution for building owners and operators.

As Martin said earlier in the call, we will continue to remain opportunistic yet disciplined with M&A. If there are not opportunities that meet our acquisition criteria, we are content to buyback our shares because we know the most about APi and what its future offers. We have great confidence in the business and the direction we're heading. We remain confident in our previously stated long-term value creation targets, and are excited about our recently announced new goal of 13%-plus adjusted EBITDA margins by year-end 2025.

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With that, I'd now like to turn the call back over to the operator and open the call for Q&A. Thank you.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from the line of Andy Kaplowitz of Citigroup.

Andrew Kaplowitz
Analyst, Citigroup Global Markets, Inc.

Q

Hey. Good morning, guys.

Russell A. Becker
Chief Executive Officer, President & Director, APi Group Corp.

A

Hey, Andy. How are you?

Andrew Kaplowitz
Analyst, Citigroup Global Markets, Inc.

Q

Good. How are you? Russ, could you give us a little more color regarding your core Safety Services markets. You mentioned the resiliency in data centers fulfillment and you've talked about healthcare before driving your safety business. But are you seeing more general recovery at this point across your customer base? Is inspection beginning to accelerate, given reopening? And are you seeing customers who pulled back in the pandemic starting to spend again?

Russell A. Becker
Chief Executive Officer, President & Director, APi Group Corp.

A

So yes, I would say, the reality of it is, Andy, is that our customers, specifically our customers in data centers, in semiconductors really have not pulled back even through the course of the pandemic and many situations have accelerated during the course of the pandemic, as more and more people were working remotely and such. There is a piece in President Biden's proposed infrastructure bill that was specific towards the semiconductor space. We're seeing a lot of activity in that arena right now.

And I think the most important thing for us is to be prudent, as we see these opportunities come forward because in a people-centered business like ours, we need to make sure that we're deploying our field leaders in a fashion that we can maximize the return for our shareholders. And that means we can't be everybody's solution and we need to be super selective as we go forward. Speaking specifically to your question around inspections, we saw really good solid inspection growth in the first quarter, north of 10%.

And so, we feel really good about our priority and our focus on continuing to grow inspections because we know that we're going to generate $3 to $4 of service from every dollar of inspection revenue that we generate. So, the answer to that question is yes. And we think that we're going to continue to accelerate that growth as we continue to build out our sales force under Courtney Brogard's leadership. And hopefully, you got a chance to see the energy and the enthusiasm that she brings based on her 15 minutes or so during the Investor Day. She's outstanding.

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Andrew Kaplowitz
Analyst, Citigroup Global Markets, Inc.

Q

Yeah. No, it's great to hear on inspection. So Russ or Tom, maybe you can talk to us about how much weather impacted margin, especially in Specialty Services and then sales in Industrial? I know you had talked about Industrial being down 30% for the year. Q1 obviously was a little lower than that. But do you see Industrial recovering? And then, can you give us the discrete impact on margins in Specialty?

Russell A. Becker
Chief Executive Officer, President & Director, APi Group Corp.

A

Well, we don't have it itemized and broken out. Really, I mean all I can tell you is that like it wasn't just Texas; it was really across the south and the southeast all the way up through New Jersey. Like we had a period of time in New Jersey where we have a significant presence where there was 30 inches of snow that our people were dealing with. And really the way we generate revenue and make money is by burning man hours. And it was very difficult for us to get people to work in the field. When we got people in the field, it was very difficult for them to be productive. That would be nearly impossible for us to really truly quantify, to be honest with you. So, I don't think it would be fair for us to do so.

Speaking of Industrial Services, I just want to start by reminding everybody, that is about 7% of our total revenue. It's a very, very small piece of our business. It's probably the piece of our business that has faced some of the greatest headwinds because of COVID. And we have some unique opportunities for us in front of us right now that we're continuing to work through and we remain optimistic that the back half of the year is going to be as guided.

Andrew Kaplowitz
Analyst, Citigroup Global Markets, Inc.

Q

Russ, maybe ask you one follow-up there. Like if I think then about your guidance for the year, you didn't change it on the revenue side. Does it maybe slant a little bit more toward Safety and Safety doing a little bit better than you thought and Industrial little worse or should we just think status quo?

Russell A. Becker
Chief Executive Officer, President & Director, APi Group Corp.

A

Well, I would think about it from more of a status quo perspective, Andy. But again, I want to go back to – Industrial is about 7% of our total revenue. It's just such a small piece of our business that we work it; we work every piece of our business. It's like having multiple children in your family, right? And I've heard Jim used this analogy a number of different times. And every one of your kids is in a different place and not every kid is as healthy as the other one. And you still need to give the right level of attention. And I think that's a really good analogy when you look at a company like us with 20-plus businesses and [ph] crossed it. (00:27:42)

And the Safety Services and Specialty Services, both have tremendous opportunities in front of them; and the backlogs are good. And really there's just one aspect of Industrial Services that is driving the majority of our attention. That business we are continuing to push towards the integrity side of the space. And that's inertia, and that takes some time to move there. You don't just flip that switch. And one day you're focused on, say, capital project-related work and the next day you're 100% focused on integrity in service-related work. It takes energy, effort, and pushing in order to get there and that's exactly what we're doing right now.

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Andrew Kaplowitz
Analyst, Citigroup Global Markets, Inc.

Q

Thanks, Russ.

Operator: Your next question comes from line of Markus Mittermaier of UBS.

Markus Mittermaier
Analyst, UBS AG

Q

Yes. Hi. Good morning, everyone.

Russell A. Becker
Chief Executive Officer, President & Director, APi Group Corp.

A

Hey, Markus.

Thomas J. Lydon
Chief Financial Officer, APi Group Corp.

A

Hi, Markus.

Markus Mittermaier
Analyst, UBS AG

Q

Hey. Good morning. Maybe I can just follow up here. And I know you guys track labor hours. Across your various businesses, how did those develop throughout the first quarter and what was sort of the exit rates into the second quarter? Thanks.

Russell A. Becker
Chief Executive Officer, President & Director, APi Group Corp.

A

Well, I mean labor hours, it's really interesting. I'm not answering your question directly right now, but I was looking at the National Fire Sprinkler Association tracks labor hours for the industry. And I was looking at some of that data yesterday and how hours continue to, so to speak, climb and decline back, but haven't achieved, say, where they were at in 2019. And our hours are really tracking in a very similar fashion to that, probably a little bit in front of that.

We have aspects of our business that were more impacted by COVID than others. So, like if you look at [ph] SK and (00:29:50) Europe and Scandinavia and including the UK, they're just starting to come out of really complete lockdown mode. And so, they've been further dampened by COVID than say the US. Canada, specifically Ontario and Manitoba not far behind, just four weeks ago went into complete lockdown.

And as part of that lockdown, I mean they – even if you were deemed essential, there was even more restrictions from that standpoint. And I felt like our hours held up – don't take this wrong way, but like surprisingly – they were surprisingly solid even with the increased lockdowns that we saw in our Canadian business. So, our hours are ticking up. We're not back to where we are in 2019, but we continue to show really good progress.

Markus Mittermaier
Analyst, UBS AG

Q

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Great. That's helpful. And then maybe one for Tom. You touched upon this briefly in your prepared remarks around the conversion rate on the cash flow, 38%. Can you maybe give us a little bit of a finer insight here on the moving pieces? I realize CapEx is up a bit, working capital swings, but is there anything especially related to industrials this quarter? Because I would have expected that the positive trends that you've seen in Safety and Specialty and the short project duration particularly in Safety, that cash would have been maybe a much better in – but maybe help us out here sort of the moving pieces and then how you see that track, maybe, early in Q2?

Thomas J. Lydon
Chief Financial Officer, APi Group Corp.
A

Yeah. So, we generally anticipate that we'll use cash in that first quarter. It is a period where we're taking care of – our capital expenditures tend to be a little stronger in that first quarter, as we get ready for the year. And so, that we have all the equipment that we need for the peaks of second, third and the first part of fourth quarter. So really tracked kind of where we thought it would be, nothing really surprised us in the quarter related to it, Markus.

Markus Mittermaier
Analyst, UBS AG
Q

Okay. Got it. I'll get back in queue. Thank you.

Operator: Your next question comes from the line of Andy Wittmann of Baird.

Andrew John Wittmann
Analyst, Robert W. Baird & Co., Inc.
Q

Hi, guys, and good morning. Thank you for taking my questions. I feel like we've talked to you guys a lot with kind of on earnings call not that long ago, Investor Day. So, just maybe a couple of clarifications here today and, I guess, maybe I'll build on the free cash flow. And Tom, specifically in the prepared remarks, you said this is a bit of a hybrid year. I don't know [indiscernible] (00:32:38) but I'm not really familiar with that. Can you just describe what you mean by that?

I understand that last year was really strong. The adjusted free cash flow conversion was like 115%. Is that basically implying that this year you're going to kind of equalize out to maybe the long-term 80% target probably under that [ph] 8% (00:32:57) target? Maybe just a little bit more detail on what you mean by that comment? Thanks.

Thomas J. Lydon
Chief Financial Officer, APi Group Corp.
A

I think that's fair. As we talked about, as we come back with stronger revenues, as we climb back, we're going to use that building working capital. And so, as we've talked, it's kind of an average rate that 80% and we were so strong last year; we're going to be on the other side of that this year. And so, we'll be building working capital as we march through the year.

We do have activities in place to work to continue to improve our working capital, by working on DSO, our inventory, our contract asset and liability processes, as well as working with our vendors on our payable terms to help mitigate what will occur there naturally. But it's positive for us that our working capital will grow and put some pressure on free cash flow this year.

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Russell A. Becker
Chief Executive Officer, President & Director, APi Group Corp.
A

Yeah. I'm going to...

Andrew John Wittmann
Analyst, Robert W. Baird & Co., Inc.
Q

Got it.

Russell A. Becker
Chief Executive Officer, President & Director, APi Group Corp.
A

Andrew, I'm just going to follow on Tom's comment there, like, it's positive. For us, we want to be using some cash this year as the business climbs back to a return to, I guess, normalcy. And so, like it gets me a little bit excited when I see – we monitor cash on a daily basis. So, we see – across all aspects of our business Europe, US, Canada. And so, we see who's using, who's not using, et cetera. And it's exciting for us when we see a little bit of cash going out the door right now. So, you should view that as being positive.

Andrew John Wittmann
Analyst, Robert W. Baird & Co., Inc.
Q

Yeah. [indiscernible] (00:34:29) just wanted to make sure that we're understanding what you're trying to say there. So, that makes all the sense in the world. I guess, just a couple of other things just so that I can understand or we can all understand the quarter's results a little bit better. The corporate EBITDA segment results was a little bit lighter than I think – we talked to you about, maybe we talked to you offline that it was going to be a little bit higher than this.

I was wondering, Tom, if there's anything in the corporate segment EBITDA coming in $80 million this quarter that was unusually low this quarter? And maybe what your expectations for the corporate expenses are going to be for the year, so we can model that correctly?

Thomas J. Lydon
Chief Financial Officer, APi Group Corp.
A

Yeah. So, we still feel good about that going forward. We had a couple of things in the quarter. One, [ph] G&A (00:35:11) didn't come back as much as we had budgeted for, as COVID stayed stronger on us. Russ mentioned, Canada and Europe, in particular, very strong lockdowns and we still had some restrictions here in the US. So, that didn't come back as strong. We also have some open critical needs that we're looking to hire in various aspects here in our corporate cost structure. And we have those budgeted coming in earlier in the quarter; and with COVID it's made hiring a little bit slower than normal. And so, that didn't come through as well. And so, those are the main drivers.

Andrew John Wittmann
Analyst, Robert W. Baird & Co., Inc.
Q

Got it.

Thomas J. Lydon
Chief Financial Officer, APi Group Corp.
A

And so, we'd expect those to rebound.

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Russell A. Becker
Chief Executive Officer, President & Director, APi Group Corp.

A

But Andy, that $20 million to $22 million a quarter is a good number. It's just a little bit in our favor. And as you pointed out, interest expense was a little bit higher in the quarter. And I think our share count is probably also higher in the quarter than most of you had. I think consensus is around $197 million, whereas the weighted average for the quarter was $200 million. And I think in Tom's comments, we're projecting that the weighted average share count will be about $205 million at year-end.

Andrew John Wittmann
Analyst, Robert W. Baird & Co., Inc.

Q

Okay. Good. I think that's all I have for now. Thanks a lot, guys.

Russell A. Becker
Chief Executive Officer, President & Director, APi Group Corp.

A

[indiscernible] (00:36:33).

Operator: Your next question comes from the line of Julian Mitchell of Barclays.

Julian Mitchell
Analyst, Barclays Capital, Inc.

Q

Hi. Good morning. Maybe just wanted to understand a little bit the EBITDA margin outlook. So I think in the first quarter, the EBITDA margin was up about 20 bps year-on-year. It looks like the guide for the year embeds around that level of increase as well, at least at the midpoint. So just wondered why you wouldn't see a bigger step-up in the balance of the year. You'll have less weather headwinds – less of a headwind from Industrial winding down easier comp, because you get into COVID year-on-year comparisons. And it sounds like you're confident on price cost not being a big headwind. So maybe help me understand kind of what the headwinds are versus all those improvements relative to Q1 for the rest of the year.

Thomas J. Lydon
Chief Financial Officer, APi Group Corp.

A

Yeah. Sure. Great question. You'll recall that we took significant actions last year in quarters two and three and reduced people's compensation and our 401-K benefits, et cetera, and we put those all back in in Q4. So we're going to lap those quarters here. And so that's, if you will, be offsetting to all the good news that you spoke about.

Julian Mitchell
Analyst, Barclays Capital, Inc.

Q

I see. And maybe help us understand sort of the scale of that temporary cost reversal, because for example things like P&E expenses as you said, they were narrower than you thought in Q1, probably narrower in Q2 as well. So maybe help scale that for us.

Thomas J. Lydon
Chief Financial Officer, APi Group Corp.

A

Yes. So, I think last year we had – in the second quarter, we had about $19 million that we had attributed to the pullback of COVID-19, and in the third quarter about $13 million.

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Julian Mitchell
Analyst, Barclays Capital, Inc.

Q

Thank you. And if we look at the second quarter guidance, I didn't see much of a reference to that. Do we assume that's unchanged? Or because you had such a tough period in Q1 with weather, I think you had a 60% sequential decremental EBITDA margin? Should we expect kind of supernormal sequential incrementals now in Q2 versus what you'd guided before?

Thomas J. Lydon
Chief Financial Officer, APi Group Corp.

A

I would go with the guidance we gave you. I'm not sure I'm totally understanding the question, I apologize. But the guidance we have has factored in, what we believe, our total cost structures this quarter and gives you the good comp to prior year.

Julian Mitchell
Analyst, Barclays Capital, Inc.

Q

I see. So the Q2 guide [indiscernible] (00:39:19) the same.

Thomas J. Lydon
Chief Financial Officer, APi Group Corp.

A

Yeah. No change in our Q2 guidance.

Julian Mitchell
Analyst, Barclays Capital, Inc.

Q

Great. Thank you.

Thomas J. Lydon
Chief Financial Officer, APi Group Corp.

A

Just to qualify that, or our full year guidance.

Julian Mitchell
Analyst, Barclays Capital, Inc.

Q

Thanks.

Operator: Your next question comes from the line of Kathryn Thompson of Thompson Research Group.

Kathryn Ingram Thompson
Analyst, Thompson Research Group LLC

Q

Hi. Thank you for taking my questions today. First on supply chain. How are you managing supply chain disruptions and just overall inflation for your businesses?

Russell A. Becker
Chief Executive Officer, President & Director, APi Group Corp.

A

Yeah. Good morning, Kathryn. Thanks for taking the time to join the call today. And so, I guess, I'm going to start by just referencing the small project size, average project size that our businesses have. Safety Services on the average project size is $10,000; Specialty Services is $70,000; and Industrial Services which is larger which is

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roughly $700,000. For the most part, in Industrial Services and in Specialty Services, the client is providing the products for us to install.

And so, we have very little risk from some of the rising commodity prices. If you look at Specialty Services – I'm not saying that we don't have any exposure because that would be not true. But if you look at Safety Services that average project size, from an inspection and service, those jobs are turning so fast that you don't have great exposure to the inflationary nature of commodity prices that we're seeing today.

The other aspect of it is, is that we practice on a weekly basis and we've been providing guidance to our businesses on a weekly basis. So, we have been very proactive in protecting ourselves in our proposals and in our contracts, to make sure that we do have protection as it relates to rising costs associated with what's going on. We really haven't been overly impacted by availability. I did see a note from one of our company presidents yesterday that the Colonial Pipeline hacking situation is causing some disruption.

As an example, Huntsville, Alabama has put some limitations in like you can only get 10 gallons of gas at a time. And so, our people are managing that from an availability standpoint. But that's a very short term situation. But I feel like our communication across the enterprise has been really solid. And we've done a lot of really positive things to make sure that we're mitigating that risk.

Kathryn Ingram Thompson
Analyst, Thompson Research Group LLC

Q

Okay. Very helpful. And then getting back to the office. As companies prepare to come back to the office and the anticipated reconfiguration that will happen, could you discuss how this is an opportunity for APG? So it could be everything from fire safety to HVAC or other categories that we may not take into consideration? Thank you.

Russell A. Becker
Chief Executive Officer, President & Director, APi Group Corp.

A

Yeah. So from an HVAC perspective, our HVAC services companies are obviously trying to provide additional filtration systems and expanded filtration systems to their different businesses. Like I can use our corporate campus as an example, we have a Minneapolis piece HVAC services company that upgraded the filtration system in both of our corporate office buildings. We also had one of the largest private companies in the world who's based in Minneapolis, recently hire us to upgrade their corporate office facility and enhance their filtration system.

So without question, there's opportunities for us in that space and we're trying to do our best to take advantage of it. You have to also remember, though, with all that being said that HVAC services is not a huge piece of our business. So, those opportunities and the scale of the company are of somewhat limited. There will be some opportunities as people really, truly start bringing people back and they are retrofitting the interior layouts of their office facilities and that will have an impact on their life safety systems, and the fact that their life safety systems will still need to meet code.

But we really haven't started to experience and see a tremendous number of those opportunities. But we're anticipating that we will, as people start being more proactive in getting people to work. The governor of Minnesota, just as an example, has just recently changed his stay-at-home order and allowed businesses more flexibility to start bringing people back to work. So, at our corporate campus we have a mandate out that 50% of our employees need to be in the office next week. And then we have a phased plan to bring people back 100% by August 15. Hopefully, that goes smoothly and goes according to plan.

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We really only have one space that we have significant concerns, isn't the right way to look at it, but we – that we feel like we have to configure to make sure that we're providing a truly safe environment for all of our employees. So, in two buildings it's a relatively small ask. But we are definitely keeping our eyes on it and we do see some opportunity.

Kathryn Ingram Thompson
Analyst, Thompson Research Group LLC

Q

Okay. Great. Thank you very much.

Operator: Your next question comes from the line of Jon Tanwanteng of CJS Securities.

Jonathan Tanwanteng
Analyst, CJS Securities, Inc.

Q

Hey. Good morning, guys. Thank you for taking my question. I was wondering, what your expectations for the Industrial profitability this year was? Does it get back to profitability? [indiscernible] (00:45:47) kind of what's in the pipeline for that segment?

Russell A. Becker
Chief Executive Officer, President & Director, APi Group Corp.

A

Again, I'm going to start by reminding everybody that Industrial Services is about 7% of our total revenue. We haven't changed our guidance, as it relates to – or our expectations and where those businesses are going to be during the course of the year. So, do we expect to make money? Of course, we expect to make money. I guess, I would hope that everybody has seen how proactive we are from a leading and managing our businesses.

And we are doing everything we can to ensure that all of the right levers have been pulled to enhance the profitability of every one of those businesses. But we like the companies, we like the businesses. And again, I'd mentioned earlier, we really have one business that we're facing more macro headwinds in the segment, and they're getting plenty of attention, trust me.

Jonathan Tanwanteng
Analyst, CJS Securities, Inc.

Q

Okay. Great. Thank you for that color. Russ or maybe Martin and Jim, the M&A markets have been hot to say the least. Are you seeing any valuations stretching beyond maybe where you're comfortable? Even on the tuck-in side or perhaps the more larger, more adjacency transformational side that you've been working on, do they seem less eager to pull the trigger now that they've seen other companies go for these higher multiples? And maybe conversely, are you seeing more flows if more people are eager to cash in on the trend?

Martin E. Franklin
Co-Chair, APi Group Corp.

A

So,...

Russell A. Becker
Chief Executive Officer, President & Director, APi Group Corp.

A

Martin, [indiscernible] (00:47:25)?

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Martin E. Franklin
Co-Chair, APi Group Corp.

A

Yeah. I'll start. Maybe, I think a couple of things. First of all, go back to history of other companies that we built with acquisitions over the years. For every deal people – the public saw, there were probably 40 deals that didn't happen, most of which would pass because of the valuation. I don't think that will be much different here. This is a very fragmented space. There's a lot of, if you like, merchandise of different kinds out there.

The gatekeeper for us will always be valuation along our call list of boxes that have to be checked. But there are always opportunities to find the right things. And what we found over the years has been the [ph] property (00:48:16) markets like we're in now, some of the better companies do become available. So, we've bought businesses in both property markets and more conservative ones. But I think there are plenty of opportunities out there, where the discipline comes in is not overstretching to buy something even if one can afford it. We're all very disciplined and we'll intend to be that way. It's how we've been for the last 25 years. I don't think it's going to change now.

James E. Lillie
Co-Chair, APi Group Corp.

A

Jon, if I could supplement. At our Investor Day, we talked about how the weighted average price including the acquisition of APi itself, the average we've paid is about 7.3 times. The larger transactions will cost more, and we hope to balance those out with the more traditional deals that APi has done under Russ's leadership over the last decade or so.

So, you're going to get some price discrepancy with lower multiples paid for the smaller family-owned businesses and higher multiples paid for perhaps assets owned by families or PE firms. Yeah. And so, our focus is to be opportunistic, keep our eyes open, and make the right decisions as we move through things and be as disciplined as always.

[indiscernible] (00:49:51)

Russell A. Becker
Chief Executive Officer, President & Director, APi Group Corp.

A

And Jon, just because I need to chime in just to hear myself talk I guess. When you look at the tuck-in world, if you will, it's reasonable. That's just the best way to put it. And so, it's a combination of a lot of different things happening in the marketplace. But as we continue to look at tuck-in acquisitions, we find the multiples to be to be reasonable. We also think that we have something different and unique that is attractive to many of these family-owned businesses and that creates an opportunity for us.

Jonathan Tanwanteng
Analyst, CJS Securities, Inc.

Q

Great. That's good to hear. Russ, finally, if you could address just how are you set up to deal with an infrastructure bill, assuming one come, and just from a labor and union perspective and access to resources such as – the things that come to the supply chain. If something big comes down the pipe, are you set up to take advantage of all that at this point?

Russell A. Becker
Chief Executive Officer, President & Director, APi Group Corp.

A

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Yeah. So I like our chances, Jon. And the reason I say that is that, our core purpose of building great leaders expands to the men and the women that are leading our efforts in the field with our customers on a day-to-day basis. And there are very few people in the space that are investing in their field leaders in the same fashion that we're investing in our field leaders.

And why does that matter? It matters because I think we retain our field leaders at a higher level than our peers. And we have created an environment where people want to come and be a part of our team and be part of the APi family, and that's a unique opportunity for us. This is a super people-centered business. And I think that, you know, the people that are investing in their human capital are going to have a unique advantage, you know, as the labor markets continue to tighten up. And I really, truly believe that. And I do think that that is something that is unique for our company. And I truly believe that it creates shareholder value.

Operator: Thank you. That was our final question for today. I'll now return the call to Russ Becker for closing comments.

Russell A. Becker

Chief Executive Officer, President & Director, APi Group Corp.

Thank you very much. And I would just like to conclude, you know, our call today by thanking each and every one of you for your interest in an APi. And this is really a great company. We have so many fantastic people. I look forward to the future for each of you to further get to know us, especially once we get, you know, on the backside of the pandemic and we can see each other face-to-face because I really believe that when you get a chance to experience the culture and the values of this organization, you will see that this is a great long-term investment.

And so, again, thank you for taking the time to join us today. And thank you for your interest in APi.

Operator: Thank you for participating in APi Group's first quarter 2021 financial results conference call. You may now disconnect.

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