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TESSCO Technologies, Inc. (TESS)

Q2 2019 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good day, ladies and gentlemen, and welcome to the Second Quarter 2018 TESSCO Technologies, Incorporated Earnings 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] As a reminder, this call is being recorded.

I would now like to introduce your host for today's conference, David Calusdian with Sharon Merrill Associates. Sir, you may begin.

David C. Calusdian
President, Sharon Merrill Associates, Inc.

Good morning, everyone, and thank you for joining TESSCO's Q2 2019 conference call. Joining me today are Murray Wright, TESSCO's President and Chief Executive Officer; and Aric Spitulnik, the company's CFO. Please note that management's discussions today will contain forward-looking statements about anticipated results and future prospects. Forward-looking statements involve a number of risks and uncertainties, and TESSCO's results may differ materially from those discussed today. Information concerning factors that may cause such a difference can be found in TESSCO's public disclosures including the company's most recent Form 10-K and other periodic reports filed with the Securities and Exchange Commission.

With that introduction, I'd like to turn the call over to Murray Wright, TESSCO's President and CEO. Murray?

Murray Wright
President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

Thank you, David, and good morning, everyone. Thank you for joining us on the call today. The headline for this quarter is growth, driving strong consistent growth and managing that growth for enhanced profitability. We are

confident that our value proposition is resonating in our markets. The initiatives we put in place during the past year combined with the execution of the sales teams are driving solid top line performance.

For Q2, we achieved revenue growth of 9% representing the seventh year-over-year increase in the past eight quarters. We expect the sales momentum to continue in the second half of fiscal 2019. While we achieved 9% revenue growth, our earnings this quarter were impacted by an increase in lower-margin public carrier sales and higher service costs in the public carrier and retail markets. Our commitment to serve our project-based and large retail customers caused us to incur higher freight-in, freight-out, and other operational costs this quarter. This resulted in lower gross margins and increased SG&A expenses.

As we are growing our project-based business, we made line-level decisions to expedite shipments to meet customer needs. We've recognized improved forecasting and collaboration with our project customers will help us continue to drive revenue growth and a better bottom line.

We are implementing new operational processes to make this happen. We've been successful in executing our strategy to drive growth from the public carrier market, and we are equally confident that our operational improvement efforts will enhance profitability as well.

Now, I'd like to provide updates on what's happening in each of our markets. Our second quarter revenue growth was primarily driven by a 45% year-over-year increase in sales to the public carrier ecosystem where we saw particularly strong results from MasTec and our Tier 1 carrier customers.

Our sales team is working hard and has been successful in gaining market share. Our revenue growth is outpacing the overall market, which we believe has grown by approximately 9% this year. Our sales team is also working well with our operational teams to improve order flow and productivity across the company.

Our value proposition has become a critical differentiator for us and a key reason we have significantly outperformed the market. We understand the dynamic challenges of this space, and we are able to provide tailored solutions to satisfy our customers' needs, and I'm confident our profitability will improve over time.

Now, let me shift gears to the Integrator and Value-added Reseller market. Last year, we launched a new go-to-market strategy to position TESSCO for future growth. During the second quarter, we completed the final piece of the implementation of that go-to market strategy through the consolidation of our value-added reseller, private system operator and government channels into what we are calling our Integrator and VAR market.

Now, the sales opportunities in these markets will be managed by one regionalized TESSCO seller. We will continue to have subject matter experts on specific end user markets such as the utility and government sectors, and we are aggressively cross-training all other sales team members.

As a result, we've streamlined the business, provided better coverage to our customers and created greater alignment with our supplier partners. We're executing well with our integrators where our Ventev products complement OEM systems. Overall, our Ventev infrastructure sales were up 6% this quarter, and we are doing a better job of incorporating Ventev products into our total offer.

We're also capitalizing on growth of IoT-based solutions particularly into the utility, mining and oil and gas spaces. This week, we announced that Verizon named TESSCO as a Tier 1 value-added distributor of Verizon mobility solutions. This is another proof point that our IoT initiatives are resonating in the marketplace.

Turning to retail, sales increased 6% year-over-year. And also contributing to that growth was a 7% increase in Ventev mobile device accessory sales. The iPhone XS, the iPhone XS Max launched in September and our team executed well under pressure to get product into the hands of our customers prior to launch. We're gaining traction with several big box stores and expect to continue to develop opportunities in coming quarters. Our work in the airport channel also continues to be successful.

I mentioned in previous quarters that we are developing a services offering for our retail customers. These solutions leverage our substantial capabilities and experience in the market, and we continue to focus on that – on the growth that that has to offer. For our retailers, we are using data to drive informed recommendations, our supply chain expertise to improve productivity and reduce costs, and systemic tools to improve the consumer experience for our broad client base. We've been offering these services to our retail customers and are beginning to offer similar services to our commercial customers.

We're also making good progress in developing our strategic wholesale partnership channel where we are working with several manufacturing partners to distribute products. This effort represents a low risk, high revenue opportunity as our service is critically important to these manufacturing partners.

Looking ahead, we expect replenishment orders for the recently launched iPhone XS and [ph] Max (00:07:17) as well as the orders for the new iPhone XR that's launching today. In addition, we expect the typical robust holiday activity this quarter.

And now, I'll turn the call over to Aric for a discussion of the financial results. I'll be back to discuss where I see the business going in each of our markets. Aric, over to you.

Aric M. Spitulnik

Chief Financial Officer, Senior Vice President, Corporate Secretary & Principal Financial and Accounting Officer, TESSCO Technologies, Inc.

Thank you, Murray. Good morning, everyone. For the second quarter, revenues totaled \$158.6 million, up over 9% from the prior-year quarter. Public carriers are up by 45% and retail was up 6%. These increases were partially offset by a 2% decline in sales to the newly named Integrator and VAR market. As Murray mentioned, we completed the implementation of our enhanced go-to-market strategy due to the consolidation of our VAR, government, and private system operator markets. This new structure will help drive increased sales opportunities.

Gross profit for the quarter increased by 5% from a year ago to \$31.4 million due to higher revenues. Gross margin for the quarter was 19.8% compared with 20.6% a year ago. This margin decline is primarily due to higher freight and expenses and product mix. The freight expenses were related to the growth in the project business, primarily in the carrier market, as well as a higher portion of international air shipments of Ventev inventory that was necessary to meet customer demands.

As we have been saying, we did expect a decline in gross margins due to product mix at the lower margin carrier business – as the lower margin carrier business increases. That is what we saw this quarter with the 45% increase in carrier revenues.

As Murray mentioned, outside of freight, we've been making progress in our gross margin improvement plan. We are incorporating better price management which includes a cross-functional project team focused on systematic pricing initiatives, improving product mix outside of the carrier market with growth in both Ventev product lines this quarter and our supplier rationalization project.

Supplier rationalization helps us by focusing on fewer suppliers which means less SKUs and suppliers to manage, better purchasing power and lower excess inventory. In the last six months, we've intentionally reduced our stock supplier count by about 100.

SG&A expenses were up 11% to \$29.5 million, due to the increased freight out and other variable operations costs primarily related to large carrier and retail customers. Our weight of products shipped this quarter increased significantly, the mix of international shipments grew and we expedited more shipments to meet customer demands which impacted these variable expenses.

In addition, we had additional bad debt expense related to a few isolated instances, higher technology costs to help support the business and increased healthcare costs. Our healthcare costs vary from quarter to quarter as we are self-insured. Despite these increased variable expenses, we are managing our fixed expenses well. Our base compensation is flat compared with Q2 of last year and our revenue per employee is up 5% over that same period. As a percentage of revenue, SG&A was 18.6% compared with 18.4% of revenue last year. Net income for the second quarter was \$1.2 million compared with \$1.8 million a year ago. Earnings per share was \$0.14 compared with \$0.21 cents in the second quarter of fiscal 2018.

Turning to the balance sheet, inventory grew slightly to support the increase in the carrier business. We also experienced a corresponding increase in accounts receivable. While growth in the carrier business inherently puts pressure on inventory and receivables, our entire organization is focused on improving these measures. We have a cash conversion committee that has been specifically established to focus on improving cash flow, and we expect to see fast returns beginning in the third quarter.

I wanted to briefly touch on the tariff issue. The vast majority of our distributed products are unaffected by the current tariffs. We have received some tariff-related price increases from suppliers on certain product categories and are largely passing these increases on through the supply chain. The area most impacted by tariffs is Ventev mobility products which are largely subject to a 10% tariff that began in September. This will likely rise to 25% in January.

The tariff had no material impact on Q2 results. We are currently working with our product sourcing team including our international agent to determine the optimal pricing sourcing roadmap going forward. We are closely monitoring the tariff dynamic in the marketplace as we move forward.

Finally, we have set our dividend at \$0.20 per share with a record date of November 14 and a payment date of November 28. We continue to anticipate year-over-year growth in revenue and profitability in fiscal 2019. As we have been mentioning, while we expect considerable growth in the carrier ecosystem, this growth will likely result in lower overall year-over-year gross margin given the tighter margin nature of many of these large carrier relationships. At the same time, we are working to implement operational improvements to increase the profitability of our project-based business from the carrier ecosystem.

As we look to the remainder of fiscal 2019, we feel good about our progress and the results we're delivering across the business. We look forward to providing additional updates on future calls.

I'll now turn the call back to Murray.

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

All right, thank you, Aric. I wanted to take a moment and give you my thoughts on the business after having just passed my two-year mark as CEO. During that time, we focused major overhaul on our go-to-market strategy and organizational realignment, supplier rationalization, expense control initiatives and we've launched several new internal technology improvements. I can tell you I'm more excited today about our long-term prospects than when I first joined the company and let me share with you few of my thoughts on the longer-term expectations in each of our markets.

In the retail market, I believe we will continue to see low to mid-single digit growth which will slightly outpace the expected market growth. The initiatives we have in place are focused on new business development, creating new channels, introducing new Ventev products and growing our value-add high margin service portfolio.

I anticipate our actions will deliver improved profitability and steady growth in this market. In the public carrier ecosystem, I have shared our excitement about the growth that we see in the sector as FirstNet continues and 5G begins to roll out. As we discussed earlier, our value proposition is driving share growth for TESSCO ahead of the overall market growth.

Our total supply chain solution offering is differentiating us in this channel. This is typically project-based business, and I see double digit growth in this space continuing for the foreseeable future. As I've mentioned, this market is subject to quarterly fluctuations due to the project-oriented nature of this business.

As we saw this quarter, rapid growth in carrier business does provide occasional operational challenges. At the same time, we are confident we can execute plans to improve our efficiency and profitability on these bigger projects. And finally, I'm excited about the new Integrator and VAR market where I believe we are under penetrated. To capture this significant opportunity, we are executing on a multi-tiered growth strategy. That strategy includes the regionalization efforts that have gone well, but that there were some bumps in the road as can be expected and should provide us with an excellent go-to-market structure to best capture of the opportunity.

We've recently invested in a team of new business development professionals who bring with them deep relationships with many large customers. And finally technology like IoT-related products and new Ventev product offerings continue to create opportunities for us. I believe we will be able to grow by double digits in the very near future.

I want to leave you with three key points. First, we are focused on delivering profitable growth. We are not interested in profitless prosperity. We're going to do this in each of our three markets by balancing mix of customers, suppliers, Ventev and value-added services.

And secondly, we are driving operational and productivity improvements to support our growth. We've experienced year-over-year revenue growth in seven of the last eight quarters and sequential growth in the last six quarters. Because of this, we need productivity and operational improvements throughout the company. I would add that we've also grown earnings five of the last six quarters.

And third, we are intelligently and strategically making investments in technology, tools and resources, and driving new initiatives to enhance the customer experience and improve our productivity. Please keep in mind that we have not even experienced yet the positive impact that we know 5G will bring to the marketplace in the near future.

And with that, operator, I would like to open the call for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Your first question comes from Maggie Nolan with William Blair. Your line is open.

Maggie Nolan

Analyst, William Blair & Co. LLC

Q

Good morning. With respect to the higher service costs in the public carrier and retail markets, is this something that's just the nature of serving these markets or other things you're doing to drive down some of those freight costs?

Aric M. Spitulnik

Chief Financial Officer, Senior Vice President, Corporate Secretary & Principal Financial and Accounting Officer, TESSCO Technologies, Inc.

A

It's a combination of both. Certainly with the carrier business, it's high-volume, high-weight items that we're shipping, so it does require more freight costs associated with it. But we're trying to do what we can to reduce that including working with our customers and the vendors on better forecasting, so that we're not rushing to get orders out the door, so the expedited shipments, I think, can go down certainly as we move forward. We're also working with our freight providers to provide some opportunities for some lower-cost methods of shipping. So it's somewhat the nature of the business. We're [ph] in outstanding path (00:18:11) and we're certainly looking at opportunities to reduce those costs going forward.

Maggie Nolan

Analyst, William Blair & Co. LLC

Q

Okay. Understood. And then switching gears a little, what sort of traction are you seeing with the services offering for retail customers and for commercial customers, would you consider this to still be kind of early days?

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

A

Hey, Maggie. It's Murray. Yeah, I think that, I'm glad you asked that question because we've built out service practice groups in the company, four of them, and the retail team is leading the way. But we're clearly on the – in the early days here and in fact just this quarter we've started charging for some of our service capabilities. We believe that TESSCO has a tremendous amount of intellectual capital and we started to round that into practice groups to support the product sales and the market needs. And I'd say we should be looking forward to some good news as this starts to unfold over the next several quarters and into next year.

Maggie Nolan

Analyst, William Blair & Co. LLC

Q

And is that incorporated in your outlook for the rest of this year?

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

A

Not so much, I don't think it's going to have a material impact. When you think about services, there's a margin enhancement opportunity and we have to first validate that customers will pay for the services and we're going to approach this in a crawl-walk-run manner.

Maggie Nolan

Analyst, William Blair & Co. LLC

Q

Understood. Thanks for taking my questions.

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

A

Thank you.

Aric M. Spitulnik

Chief Financial Officer, Senior Vice President, Corporate Secretary & Principal Financial and Accounting Officer, TESSCO Technologies, Inc.

A

Thanks, Maggie.

Operator: Thank you. [Operator Instructions] Your next question comes from Bill Dezellem with Tieton Capital. Your line is open.

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

Q

Thank you. I have a group of questions. First of all, how important was FirstNet in the carrier growth here in the third quarter?

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

A

Yeah. I think, FirstNet is definitely pretty significant. Yeah. It's starting to, we've talked about this in the past, Bill, starting to gain some traction for many of our contractor customers right now.

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

Q

And how long are you anticipating the FirstNet build-out to take place?

Aric M. Spitulnik

Chief Financial Officer, Senior Vice President, Corporate Secretary & Principal Financial and Accounting Officer, TESSCO Technologies, Inc.

A

At least over the next year-and-a-half or so...

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

Q

Yeah.

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

A

Maybe longer than that too, I think.

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

Q

Yeah.

Aric M. Spitulnik

Chief Financial Officer, Senior Vice President, Corporate Secretary & Principal Financial and Accounting Officer, TESSCO Technologies, Inc.

A

Yeah.

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

Q

That is helpful. And by the time that the FirstNet rollout and let's just use that year-and-a-half and say it doesn't go past that, the timeframe. Are you anticipating that 5G will be a meaningful benefit by then or is that still a little bit too early? What I'm trying to understand is as we get out in the future, will there be a gap or does one just layer on top of the other?

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

A

I think the challenge, Bill, will be that the 5G intensity in the market level around that discussion is really starting to pick up. And without getting into a whole other discussion or commentary around what happens with Sprint and T-Mobile, but I would expect that if that closes that I think T-Mobile will be very aggressive in the marketplace, and I think that that will help to drive accelerated implementation of 5G rollouts across the company – our country, and I think we'll participate in that. But the timing, we originally thought it would start to pick up in December kind of timeframe, but I think it'll probably roll out and start to accelerate for us going into next year.

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

Q

Is that really weather-related, Murray?

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

A

I'm not so sure that it's weather-related or just getting – everybody needs to get kind of the traction and get organized for that rollout. But, I mean, your point – your question is a good question, and to answer it directly, I think that there's going to be a crossover. I think, we're going to be executing on FirstNet, and I think 5G will start to gain momentum. FirstNet will drop off into the future, and 5G will continue to accelerate for four years.

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

Q

And when you are referencing, I realized that I'm trying to dial this a little bit tightly, but 5G beginning early next year, is that the March quarter that you are thinking right now?

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

A

No, I was thinking next fiscal.

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

Q

Okay.

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

A

Beginning of the next fiscal year. So it'd be our Q1 which would be kind of the second quarter. I think we'll start to see some more activity in that kind of timeline.

Aric M. Spitulnik

Chief Financial Officer, Senior Vice President, Corporate Secretary & Principal Financial and Accounting Officer, TESSCO Technologies, Inc.

A

Yeah.

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

Q

Great.

Aric M. Spitulnik

Chief Financial Officer, Senior Vice President, Corporate Secretary & Principal Financial and Accounting Officer, TESSCO Technologies, Inc.

A

First of all, both of these projects are obviously several-year projects, and they're going to have ebbs and flows. But I think we'll probably start to see the bulk of FirstNet being done over the next 18 months. It's probably going to continue a few years after that until it's fully complete. And the same with 5G, it's going to start, for us, probably slightly slower, and then pick up as we go and then drop off towards the end.

So they're both kind of bell curves of somewhere between three and five years, and they're going to overlap somewhat. They're probably not going to be both at their peaks at the same time for us. So, I think, it will kind of FirstNet will start to drop off a little bit and 5G will pick up fairly close to that.

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

Q

Thank you. I do appreciate that extra detail. And then, Murray, you opened the door to T-Mobile. In the past, it has been my sense that you have not had a lot of business with T-Mobile. Number one, is that correct? And two, do you feel as though you are positioned better today than you have been in the past?

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

A

For T-Mobile?

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

Q

Yes.

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

A

Yes, yes and yes. I mean, we've done some business there, and we have done – in our current customer base, Sprint is a pretty significant customer for us and there's also the contractor marketplace that we support that are primarily doing build-outs for T-Mobile. And so, those are indirectly supporting the T-Mobile account which we participate in 100%. Does that make sense?

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

Q

That does make sense, yes. Thank you. And you also, in your opening remarks, had referenced that earnings have grown five of the last six quarters. I believe that next quarter, the December quarter, your hurdle is \$0.19. Are you anticipating growing over that?

Aric M. Spitulnik

Chief Financial Officer, Senior Vice President, Corporate Secretary & Principal Financial and Accounting Officer, TESSCO Technologies, Inc.

A

I think that's certainly on the table. We didn't say yes or no to that that we just talked about the entire year being better than last year. And the – for the entire year to be better, we need to at least grow more than where we are right now. So, the timing of this business, again with the carrier business being so project-related, it's difficult for us to say exactly whether that's going to be Q3 or Q4 or both. But we're confident that over the six-month period we're going to grow. Whether that's the third quarter, fourth quarter or both, we're not getting into that level of detail at this point.

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

A

Hey, Bill, I'd just like to – I'd like to pile on a little bit because I want you to have understanding of how we're viewing this. I would love to have a trajectory line that's very nice and flat that goes up into the right. The marketplace opportunities are very strong, but I don't think that we can effectively commit that a straight line is going to be the way that the trajectory of the business will go.

So, I think, that what we're seeing as we're reshaping the business and setting ourselves up for success in the future in the markets that we want to be in, we're going to hit a few speed bumps related to growth. And because some of this business is project-based, we're a little bit reluctant to say, absolutely here's what's going to happen. However, as Eric said, over the next 6 to 12 months, we're very confident that the trajectory of the business overall, both from our revenue and profitability perspective, is going to continue to improve.

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

Q

Great. Thank you. And actually on that note, doesn't – as the 5G build-out begins and you're working with multiple carriers layering on the VAR integrator group, is it's now called, I mean, you end up having multiple project, multiple drivers. And shouldn't that in and of itself smooth out that trajectory even when some are up and some are down?

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

A

Well, that was my point when I was talking a little bit about the reason that I'm so excited about the foreign integrator market is because there are thousands of – there's thousands of them.

And so to your point, it helps us balance the business better when we can gain the traction in that marketplace. In order to do that effectively, we really felt as though we needed to reorganize and reposition the company for success there. So, I feel like, with the talent that we've attracted to the team, the reorganization moves that we've made, I think that this is very exciting for the company. But right now, it's just happened. We just finished – we finished the final stages of it in the second quarter.

So, I would like to tell you it's been disruptive, and it's been difficult to make all of these changes and still trying to deliver growth and meet expectations as we've made these changes internally and positioning to the marketplace. So, we're finished with that. There's probably some tweaks along the way. But listen, we've attracted some really great talent in a business development team to the company.

We're calling on accounts that we haven't called on them before, and we're calling on them with solutions that we've never had before. And I referenced this and I've talked about the IoT piece several times. I mean, to us, it's pretty exciting but it's early. And so if you're going to hammer me for, what are you going to do in the third quarter in this market, I'd say, I'm going to need a couple of quarters to get some traction in this business, so that we can be more predictable. And then we should be more predictable in that market.

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

Q

That is really helpful. And I can either step back in queue or have a couple of more questions, just – which would you prefer?

Aric M. Spitulnik

Chief Financial Officer, Senior Vice President, Corporate Secretary & Principal Financial and Accounting Officer, TESSCO Technologies, Inc.

A

Yeah. Go ahead.

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

Q

So let's talk about that change in the go-to-market strategy from a couple of standpoints, if you would please. Number one, in the past, we have thought of the government, the VAR and the private system sales person as each having a different expertise. And you referenced having subject matter experts but then regional coverage. Can you talk through how you accomplished having one person in the region who is able to talk the language of all three of those, all three of those types of business.

And just for fun, I'll hammer you a little bit more using your term. So since your integration that go-to-market strategy or change of that go-to-market strategy is now complete and you've been able to deliver growth throughout the process of changing the tire, as you're driving down the road. Doesn't that make growth easier for you now on a go-forward basis even before you truly hit your stride? So couple of different questions in there.

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

A

So let me try to sift through that, Bill, a little bit. But I think picture yourself in Spokane and the territory as a representative or a seller from TESSCO, now you have that ownership and that responsibility of that marketplace. And so what we wanted is we wanted our sellers some who would be having coming from the PSO background or some from government and some from VAR to up-level their skills, so that they could run that marketplace completely. And oh, by the way, there are experts at TESSCO to help support them when they get into opportunities that require their expertise. Do you need somebody that knows about the utility market? Do you need somebody that understands oil and gas? Do you need somebody to help you fill out an RFP for government for the city of Spokane?

And so, we feel like the ownership of that territorial market also aligns us with our vendor partners. And oftentimes our vendor partners, in fact all of them that I can think of, are all aligned in a geographic way. And so our team

was misaligned, so we couldn't work with our Tier 1 partners and, say, let's put an initiative in place. How are we going to win this business?

And I think that those dynamics are going to take us some time on the training levels, on our market coverage perspective and introducing the sellers to new accounts. All the people are still here. They're still here, but they've got different accounts that they need to cover and it's all segmented by geographic regionalization.

And as I mentioned, I think we have done – I appreciate the comment that we've done a pretty good job. I think we have. This was the final and pretty significant step in finalizing the regionalization of all of the accounts. So our team is just starting to work through new names, introducing themselves. And that's kind of the status. As I mentioned and I think you are getting to as well, it should be more predictable once we get through the learning curves that we're anticipating. So that's why I feel really good and I feel optimistic about where we're headed with this marketplace.

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

Q

Thank you for all that color, Murray. And then taking that a step further, you had mentioned that you have brought on a number of great people, good talent...

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

A

Yeah.

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

Q

...as you've done this. How costly has that been from an expense perspective? I'm trying to grasp how much we have absorbed of incremental expense that really has been unproductive because they're just getting their feet on the ground?

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

A

Yeah. And net-net, it's really non-incremental. We are able to move some things around and reduce costs in other places to invest in this new business generation talent. So, overall, the net cost adjustment is not of any significance.

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

Q

Great. That's helpful. And then I believe this will be my last question. Is there an inflection point that that you are soon approaching when you have the expenses in place, the expertise is there, and now you have this – and your gross margin has found its kind of settled in point particularly in the carrier market.

And some of these new programs that you're talking about actually lower your cost and create a little bit more robust opportunity with the gross margin where really you start to see all of these initiatives that you're discussing tied with the growth in the carrier market between FirstNet and 5G that you end up with really an inflection point where your gross profit dollars and earnings just kind of have that hockey stick.

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

A

I'd like to say that it's going to be a specific date sometime in the future, but I don't really see it working that way. The reason that we want to be as transparent as possible is, I want our investors and our potential investors to understand that we're working through a lot of positive dynamics in the company.

If they all come together, there's – I would love that. I think, it's managing growth, figuring out how TESSCO is going to manage the growth and opportunities. And I think that we're in the midst of that process. I do think, though, Bill, that a lot of the changes that we put in place in the last two years were coming out of the other end of those. And FirstNet and 5G are going to gain traction as we go into the next fiscal year, let's say.

William Joseph Dezellem

Chief Investment Officer & President, Tieton Capital Management LLC

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Great. Thank you both for the time.

Aric M. Spitulnik

Chief Financial Officer, Senior Vice President, Corporate Secretary & Principal Financial and Accounting Officer, TESSCO Technologies, Inc.

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Thanks, Bill.

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

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Thank you, Bill. Thank you for your questions.

Operator: Thank you. And I'm showing no further questions at this time. I'd like to turn the call back over to Murray Wright for closing remarks.

Murray Wright

President, Chief Executive Officer & Director, TESSCO Technologies, Inc.

Great. Thank you, Heather, and thanks to everyone for joining us today. We really appreciate your support of TESSCO. We hope to see many of you at the Southwest IDEAS Conference in Dallas where we'll be presenting on November 15; and at the LD Micro Conference where we will be presenting on December 6. I'd like to end the call by thanking all of our team members for their continued hard work and dedication. Have a great day, everyone.

Operator: Ladies and gentlemen, thank you for participating in today's conference. This does conclude the program, and you all may disconnect. Everyone, have a wonderful day.

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