140482036195

CUI Global Q4 2016 Earnings Call
March 14, 2017

C: William Clough; CUI Global; President, CEO
C: Daniel Ford; CUI Global; CFO
C: Sanjay Hurry; CUI Global; IR

P: Eric Stine; Craig-Hallum; Analyst
P: Joe Maxa; Dougherty & Company; Analyst
P: Rob Brown; Lake Street Capital Markets; Analyst
P: Amit Dayal; Rodman & Renshaw; Analyst

+++ presentation
Operator^ Good day, ladies and gentlemen. Welcome to the CUI Global's fourth quarter and full year 2016 results conference call.

(Operator Instructions)

As a reminder, today's conference call is being recorded. I would now like to introduce your first speaker for today, Sanjay Hurry, Investor Relations. You have the floor, sir.

Sanjay Hurry^ Thank you, Andrew. Good morning, and welcome to CUI Global's fourth quarter and full year 2016 results conference call. A copy of the Company's earnings press release and accompanying PowerPoint presentation to this call are available for download at the event and presentations page on the Investor Relations section of the CUI Global website.

With us on the call this morning are William Clough, President and Chief Executive Officer; and Daniel Ford, Chief Financial Officer. The purpose of today's call is to review the Company's financial results for the fourth quarter and full year, and to provide you with a look ahead to fiscal 2017. Following management's remarks, the call will be opened to question and answers.

A telephonic replay of this call will be available until March 28. You may also access the archived webcast and accompanying PowerPoint at any time on the Investor Relations section of the CUI Global website.

As a reminder, this call will contain certain forward-looking statements within the meaning of the Section 27A of the Securities Act of 1933 as amended, and Section 21E of the Securities and Exchange Act of 1934 as amended. Such statements are subject to risks and uncertainties that could cause actual results to vary materially from those projected in the forward-looking statements.

The Company may experience significant fluctuations in future operating results due to a number of economic, competitive, and other factors, including among other things, our reliance on third-party manufacturers and suppliers, government agency budgetary and political constrains, new or increased competition, changes in market demand, and the performance or liability of our products. These factors and others could cause operating results to vary significantly from those in prior periods and those projected in forward-looking statements. Additional information with respect to these and other factors, which could materially affect the Company and its operations, are included in certain forms the Company has filed with the Securities and Exchange Commission.

With that, I'd like to hand the call over to William Clough, Chief Executive Officer. Good morning, Bill.

William Clough^ Thank you, Sanjay. Good morning everyone and thank you for joining us on our fiscal fourth quarter and full year 2016 results conference call. I am pleased to be speaking with you following our announcement of several new developments this morning, in addition to reporting our fourth quarter and full year 2016 results. These developments are but a few of the reasons why I believe that 2017 is truly a transformational year for CUI Global and its technologies.

Let me begin. Earlier this morning we filed a shelf registration that, once declared effective by the SEC, gives us the flexibility to raise capital up to $100 million with at-the-market continuous offering program, or ATM, of common stock in the amount of $30 million. I will discuss this strategic filing in greater detail after Dan's remarks, but in brief, we are preparing to aggressively enter the acquisition market, specifically in the North American energy sector. While we have no immediate plans to issue stock this registration allows us to operate from a position of strength as we pursue our M&A strategy, and this ready access to capital ensures that we can do so in an expedient manner.

Our second announcement this morning is the formation of a strategic partnership with ENGIE, the French energy giant. With this partnership we gain access to ENGIE's customers in not only its home country and in the rest of Western Europe, but also in North America and Asia. ENGIE is one of the titans in the energy industry with over $75 billion in annual revenue, and they have chosen to partner with us.

Now let me provide some context on the past year. We entered fiscal 2016 with the promise of a disruptive technology applicable to the global natural gas industry. While our GasPT fiscal monitoring solution had gained traction among early adopters, we had yet to secure an anchor customer whose deployment would validate our solution to that industry. In our electronics business, the acquisition of Tectrol in 2015 enhanced our capabilities and broadened our customer base. Going into 2016, we were determined to leverage our combined capabilities, product offering and unmatched customer service and support to pursue partnerships with some of the largest and most recognized leaders in the electronics distribution market and further broaden our base of business.

Flash forward to today and we have improved our business during 2016 strategically and operationally. We enter 2017 having expanded market awareness and increased adoption in both of our business segments, setting us up for growth both in the near and long term.

Let me briefly recap key developments in 2016 that sets the stage for our growth in 2017. In our electronics business, there were several positive developments to note in 2016. First, our partnership with Virtual Power Systems on the ICE Block product line has progressed rapidly since its formation a year ago. To remind you, we believe that ICE Block sets a new standard for an efficient power infrastructure utilizing software-defined power that brings the benefits of elastic power to data centers. We are in the initial stages of commercializing this product line, and after the close of the fourth quarter, we announced that initial ICE Block units were successfully deployed for testing with industry-leading data center operators, including a Fortune 500 company, a Fortune 100 company that is also one of the largest technology providers in the world, and also with a top tier data center hardware provider. We have since added a fourth unit for testing with one of the largest e-commerce platforms in the world.

Second, in the fourth quarter, we secured Arrow Electronics as a distribution partner. This new partnership speaks to our technical capabilities, brand strength and the depth of our offering. In all we now count four of the largest electronics distributors in the industry as partners. This partnership went live in January and I am pleased to report that Arrow has already begun to reorder products from us. As ours is a sell-through relationship this evidences strong receptivity to our products by Arrow's customer base and will result in revenue recognition in 2017.

In general, we are seeing improving demand trends in the electronics market. Our largest distributor, Digi-Key, has increased order flow for several consecutive months, order flow that we haven't seen in over a year.

Third, our direct sales efforts are bearing fruit. After the close of the quarter we announced a $1. 6 million order with a new customer that demonstrates this business segment's continuing ability to acquire new customers and close contracts of material size. Power and Electromechanical backlog at quarter-end stood at $18.1 million.

Turning to our energy business, for those of you who have been long time investors in CUI Global, you are aware that it took four years to overcome regulatory and certification hurdles to acquire our first anchor customer for our industry shifting technology, the GasPT. I am very pleased to say that it has only taken one year since the addition of Snam Rete to add three more anchor customers. They are SGN, National Grid, and as of this morning, ENGIE.

These new customers reflect shorter sales cycles following our Snam Rete award and is in line with our expectation of how penetrating the EU market first with its unified regulatory scheme would lead to faster uptake of our products. Our ability to deliver accurate and reliable system metering solutions to this market is uncontested. Simply put, the technology works and does exactly what we said it would, and the marketplace knows this.

In fact, our GasPT solution has not failed a single test or field trial. With respect to Italy, the regulatory hurdle we have talked about before is outstanding, and there is no timetable on a resolution at this time. A number of GasPT units have been successfully installed in the field, and I am pleased to say that Snam Rete is reporting a significant increase in revenues as a result of accurately measuring and billing for the gas being used. We still expect that Snam Rete will resume its delivery schedule of 1,200 units per year immediately after the regulatory issue is resolved.

Staying with our energy business, the gas industry's expanding use of bio-methane to grid is catalyzing demand for our GasPT and biomethane skids. Biomethane to grid is one segment of the market in which our Orbital subsidiary in the UK has a commanding market presence. As more utilities adopt alternative fuel sources and green gas, demand for biomethane to grid systems that can accurately measure the injection of renewable gas into the pipeline is growing. Orbital's ability to design, manufacture, deliver and commission these systems that include our GasPT and VE sampling solution is filling that demand.

To date we have successfully delivered 17 biomethane to grid systems. In an interesting development, Ofgem, the government regulator for gas electricity markets in Great Britain has issued a potential regulatory request, called the Ofgem letter, to change the gas accuracy level requirements on the UK network so that they can begin to use the GasPT for fiscal metering at smaller metering stations, and particularly for metering on biomethane skids. SGN and National Grid are already using GasPT on their larger off-takes. In fact, the Ofgem letter specifically names our GasPT solution as the reason behind the proposed regulatory change.

You can find a copy of Ofgem's regulatory notice on our website under the media room page. By relaxing the regulatory requirement for accuracy, Ofgem seeks to reduce infrastructure costs, specifically costs associated with biomethane. Once approved, Ofgem will recommend GasPTs across the board both on biomethane to grid and on smaller off-takes. What this means to CUI Global is that once approved our European and UK customers will be able to replace gas chromatographs with our GasPT simply because the economics favor our solution.

From our perspective, there is no alternative product that can match our total cost of ownership, speed or efficiency. We are now awaiting official notification of the regulatory change. The Ofgem letter is another example of global trends in the gas industry to make gas measurements cheaper, faster and more accurate. From a business development perspective adoption of our GasPT because of the Ofgem letter should bolster our profile in similar opportunities across continental Europe.

Unlike fiscal monitoring in Western Europe, our value proposition in North America is centered on effective and efficient process control. Critical to our penetration of this geography is Daily Thermetrics, with whom we established a partnership for our VE sampling system. As a manufacturer of our VE-Probe and reseller, Daily Thermetrics is short-circuiting our path to the region's major gas operators. Very shortly we will be collaborating with Daily Thermetrics on a joint test at a Scotia Gas facility that is designed to record data that evidences our superior probe design relative to what is currently available to the industry.

We believe this data will make a very effective sales tool to Daily Thermetrics' installed customer base. In fact, we have already attracted the attention of a multinational operator, the very same Fortune 100 operator with whom we have previously worked in Australia, who asked to be on-site at the testing ground to evaluate our solution with Daily Thermetrics. The opportunity with this one operator alone could be material to us. We are also moving to penetrate big gas operators in North America with our GasPT solution.

Our efforts to secure certification and move forward with a major Canadian operator is moving more slowly than we would have liked. Still, our GasPT is forcing a change in the institutionalized method of measuring gas and while we cannot control the timing of that change it is our expectation that based on the cost, efficiency, speed and accuracy of our GasPT solution this will happen.

New awards in the quarter to our energy business segment drove segment backlog to $12.1 million. From a strategic perspective you can see that we have made a lot of progress over the past year. Operationally, we have also made significant progress. Our calibration and testing center at our Orbital facility in the UK can deliver GasPT devices at volume to support our growth goals. Further, our new office in Houston gives us the infrastructure to further our penetration of North America.

Subsequent to the close of the quarter, our energy subsidiary in North America was awarded the prestigious ISO 9001-2008 quality management certification. This accreditation expands our addressable market and enables us to bid on larger opportunities in this sector.

Dan will review our financial results in a moment, but I want to offer a few highlights of the year.

In 2016 we made tremendous strides in executing on our strategy to drive growth. For the year, we reported revenues of $86. 5 million essentially unchanged from last year. This top line performance however masks an underlying broadening of adoption of our GasPT solution that has in just one year moved well beyond Italy into the UK, and now for those who have seen this morning's ENGIE press release, further into Western Europe, and quite possibly Asia with the backing of one of the global energy icons.
We have also made tremendous strides in working capital. We improved cash flow from operations by $5. 6 million and are now just under $1 million negative compared to a negative $6.4 million in 2015. We exited the fourth quarter with a cash on hand of about $4. 6 million.

I'll now turn the call over to Dan, our CFO, to review our financial results for the quarter and year in greater detail. I will then conclude the call with a look ahead to fiscal 2017 after which I will open the call for Q&A. Dan?

Daniel Ford^ Thank you, Bill. Let me take you through the financials for both the fourth quarter and year ended December 31, 2016. We are reporting total revenues of $19. 4 million for the fourth quarter of 2016 compared to $21. 9 million in the fourth quarter of 2015.

Power segment revenue for the fourth quarter of 2016 was $13.8 million compared to $14. 4 million during the same period last year, representing a 4% drop from the fourth quarter in 2015. The drop in revenue was due to lower revenue from CUI Canada related products compared to the previous year. Revenue from the Energy Segment for the fourth quarter of 2016 was $5.6 million compared to $7.5 million in the fourth quarter of 2015.

The decline in the energy segment revenue compared to the fourth quarter of 2015 was due to the ongoing regulatory issue in Italy that resulted in no shipments of our GasPT solution to our customer there, and the continued lower foreign currency translation in Orbital UK due to drop in value of the British pound following the Brexit vote in June. Revenue for the full year ended December 31, 2016 was flat at $86. 5 million compared to $86.2 million in the same period in 2015.

Revenue breakout by business segment for the year was $58. 4 million for the Power and Electromechanical segment compared to $58. 0 million in 2015. The energy segment revenue was $28. 1 million in 2016 compared to $28. 2 million in 2015. Using the same foreign-currency translation rates in 2016 the Orbital UK results would have improved significantly, approximately $2. 8 million higher and our consolidated net loss would have been approximately $75,000 lower had we used constant currency exchange rates in 2016 as in 2015.

Revenue for the three months and year ended December 31, 2016 are attributable to continued sales and marketing efforts, sales through distribution channel customers, the CUI Canada related product line additions and the revenues generated since the January 2015 opening of Orbital Gas Systems, North America.

The cost of revenue for the three months ended December 31, 2016 was $12. 9 million compared to $13. 4 million in the same period last year. As a percentage of revenue, the cost of revenue increased to 67% in the fourth quarter of 2016 from 61% during the prior-year comparative period.

As a reminder, this percentage will vary based upon the Power and Electromechanical product mix sold, the mix of natural gas systems sold, contract labor necessary to complete gas related projects, the competitive markets in which the Company competes and foreign exchange rates.

The cost of revenue for the year ended December 31, 2016 was $54. 2 million compared to $53. 9 million in the same period last year. As a percentage of revenue, the cost of revenues remained constant at 63% in 2016 and 2015. The cost of revenue as a percentage of revenue reflects improved product mix, including an increased volume of higher margin GasPT sales within the Energy segment, offset by lower margins in the Power and Electromechanical segment.

As a result of the improved product mix in the Energy segment, for the year ended December 31, 2016 the cost of revenues as a percentage of revenue dropped 5 percentage points from 63% to 58%. This improvement helped to offset lower margins incurred in the Power and Electromechanical segment as that segment's cost of revenues as a percentage of revenue increased slightly to 65% from 63%.

Gross profit for the quarter ended December 31, 2016 was $6.5 million, or 33%, compared to $8. 5 million, or 39%, in the same period of 2015. For the year ended December 31, 2016 gross profit was $32.3 million with a gross margin of 37%, unchanged from last year. During the three months and year-ended December 31, 2016, the Power and Electromechanical segment generated gross profit margins of 32% and 35%, respectively, while the energy segment generated gross profit margins of 36% and 42%, respectively.

For the three months and the year-ended December 31, 2016, SG&A decreased $0.6 million and increased $1.2million, respectively, compared to the prior-year comparative period. The decrease for the three-months ended 2016 was largely due to decreased corporate SG&A due to lower employee expenses, including bonuses and severance and lower professional fees. The energy segment also decreased in the quarter due primarily to lower translation rates at Orbital UK as the average translation rates for the British pound in the fourth quarter of 2016 dropped 18% compared to the average translation rate in the fourth quarter of 2015. The increase for the year is largely due to $0. 6 million in severance cost incurred in the Power and Electromechanical segments for the transition of the R&D team to CUI Canada, and for various positions within the Energy segment.

Increased audit and accounting fees in the year ended December 31, 2016 of $0. 7 million contributed to the increased SG&A. Other increases in SG&A during the year were associated with the ongoing activity to reach new customers, promote new product lines, including Novum, ICE Block, GasPT, IRIS and the VE-Probe, as well as new product introductions partially offset by a foreign currency translation at Orbital UK.
Further to the partially offsetting the increased SG&A was a $0. 3 million decrease in non-severance related SG&A associated with the activities of Orbital Gas Systems, North America, was opened in January 2016 and had increased product related costs in its first few months of operations. SG&A increased to 40% of total revenue, compared to 38% of total revenue during the year-ended December 31, 2016.

The Company reported a net loss of $2.6 million or $0. 12 per share for the quarter ended December 31, 2016 compared with a net loss of $1.3 million or $0.06 per share in the prior year period. For the year ended December 31, 2016, the Company reported a net loss of $7.3 million or $0.35 per share compared to a loss of $6 million or $0.29 per share in the prior year period.

The increase in the net loss for the three months ended December 31, 2016 compared to the three months ended December 31, 2015 was due to lower revenues and resulting gross profits in the three months ended compared to the prior period. The increase in the net loss in 2016 compared to 2015 for the full year was primarily the result of increased selling, general and administrative expenses and increased tax expense.

Earnings before interest, taxes, depreciation and amortization or EBITDA for the three months and year-ended December 31, 2016 were a loss of $1.8 million and $3.9 million, respectively. EBITDA for the three months and year ended December 31, 2015 was a loss of $0.5 million and a loss of $2.7 million, respectively.

Adjusted EBITDA for the three months and year ended December 31, 2016 were a loss of $2.3 million and $3.2 million respectively. The prior year adjusted EBITDA for the three months and year ended December 31, 2015 were a loss of $0.3 million and $1.3 million, respectively.

Adjusted net income or loss, which represents net income or loss plus the amortization expense of the intangible assets acquired via the 2015 Orbital acquisition and the 2015 CUI Canada acquisition, plus the expense associated with stock and options issued for compensation, royalties and services, for the fourth quarter of 2016, was a loss of $2.6 million. This compares to an adjusted net loss of $0.7 million for the fourth quarter of 2015. For the year ended December 31, 2016 adjusted net loss was $5.2 million compared to an adjusted net loss of $2.9 million in the comparable prior year period.

At December 31, 2016, CUI Global held cash and cash equivalents of $4.6 million, a decrease of $2.7 million since December 31, 2015. Operating requirements generated negative cash flow from operations of approximately $0.8 million during the year ended December 31, 2016, which was a $5.6 million improvement from negative cash flow from operations of $6.4 million during the year ended December 31, 2015. The use of cash from operations in 2016 was benefited by improved accounts receivable balances in both business segments at December 31, 2016 compared to 2015 as a result of improved collections in both segments and for the transition of Tectrol customers to CUI Canada that had delayed some payments at the end of the prior year.

CUI Canada's cash from operations improved significantly from 2015, while Orbital Gas Systems, North America, continues to use more cash than it produces due to the cost of establishing the Orbital brand in the US. As that business matures, we expect it to be [cash positive] in the short-term. Orbital UK's cash from operations improved significantly in 2016 compared to use of cash from operations in 2015. Overall, the change in cash used in operations is primarily a result of the net loss in 2016 before non-cash expenses affected by changes in assets and liabilities.

During 2016, in addition to the change in trade accounts receivable, significant factors that impacted cash used in operations included cash used for inventory purchases, that increased approximately $1.7 million associated with pending customer orders and ongoing projects. Changes in costs in excess of billings were approximately $1.3 million, use of cash in the period related to billings on some projects in the energy segment and unearned revenue increased $1.2 million primarily in relation to increases in deferred revenue from the distributor activity within the Power and Electromechanical segment. CUI Global reported two non-cash entries of $0.3 million per inventory reserves partially offset by $0.1 million of an unrealized gain from a derivative.

Finally, with regard to the filing of our S-3 and ATM this morning, we expect that our 2017 capital needs will be financed through available liquidity as well as capital commitments that we have already secured through our line of credit and the opportunity to borrow against our facility in the UK if necessary. While we did not have any near term requirements for equity capital, we believe it is prudent to keep these tools available to us as we continue to manage and grow our business going forward.

This concludes my prepared remarks. I will turn the call back over to Bill. Thank you.

William Clough^ Thank you, Dan. As I noted at the start of this call our strategy in 2016 was to build awareness and increase adoption of our energy solutions to drive growth. In 2017, we intend to continue along the same path while converting opportunities borne out of our efforts last year into revenue this year. Our opportunity set in 2017 shows clearly the progress we have made in just a year's time. Let me spend a few minutes articulating our priorities and our opportunities this year.

To begin, we will continue to drive adoption among the top tier of gas operators globally. The ENGIE opportunity we announced this morning is truly remarkable in terms of its scope and its potential impact to CUI Global. Our agreement spans our GasPT and VE sampling technologies for deployment in natural gas and green gas opportunities within ENGIE's installed customer base and especially in Asia, where it has its significant presence, and to prospective customers.

As a thought and technology leader and an active proponent of sustainable energy our partnership with ENGIE validate our solutions as a means of fiscal monitoring that is far more efficient and cost effective than those currently deployed by the gas industry. The opportunities with and through ENGIE are considerable. Through its integration subsidiary, ENDEL, ENGIE expects to deploy as many as a 1000 biomethane to grid skids over the next several years.

Use of our GasPT device and our significant expertise in that market silo will only enhance ENGIE's ability to deliver on their commitment. ENGIE operates one of the largest LNG supply chains in the world, including a fleet of 14 LNG tankers. Our LNG application developed in conjunction with the Cryostar group several years ago is perfectly suited to analyze pressurized natural boil-off gas and provide composition data that will enable ENGIE to use LNG as a fuel source for its fleet of natural gas tankers.

With our five-year GBP30 million framework agreement with National Grid in place, we have an opportunity to further penetrate National Grid in a much more significant way than we have achieved to date. Our framework agreement encompasses products and services including IRIS, GasPT and our VE system, so there is tremendous opportunity up-sell and cross-sell our energy product offering to them.

With SGN, our project to bring GasPT down to the retail level for residential customers with DNV GL is progressing. ENGIE has also shown strong interest in deploying GasPT at the retail level. It is early days, but the opportunity with both SGN and ENGIE could be a substantial one for CUI Global.

Next, we are focused on our continued penetration on the North American market. In addition to opportunities in North America now afforded us through ENGIE who owns and operates among other facility, the longest operating LNG terminal of its kind in Everett, Massachusetts. We are also leveraging our leadership position in biomethane to grid in the UK to take advantage of similar business trends states side.

Our competitive advantage is our ability to deliver a biomethane to grid solution cheaper because of the GasPT. No one else can offer this solution. We have bids out for biomethane skids in several US states and Canada.

Our third priority is to penetrate new geographies for our energy products. By way of example, our relationship with ENGIE may yield our first foray into the Asia Pacific energy market.

ENGIE has discussed taking us into China where ENGIE among other things operated 30 million customer pipeline in Chongqing, entered into a 4-year contract in 2013 to deliver 2. 3 million metric tons of LNG to China over a 4-year period and is developing in conjunction with PetroChina, six underground gas stores sites with a combined capacity of 10 billion cubic meters of gas. To put this into perspective, this is equivalent to the total storage volume available in all of France.

To conclude, as we enter fiscal 2017, we are beginning to see results of our relentless pursuit to drive market awareness and adoption in both of our business segments. This is especially evident in our energy business where momentum continues to build and we look for this traction to positively contribute to both top and bottom-lines moving forward into 2017 and beyond.

We are a company born of technology acquisitions and new product introductions to new markets to drive growth. With growing adoption of our disruptive energy solutions and expanding roster of blue-chip operator-customers in the filing of our Form S3 this morning reflects our belief that the time is right to leverage our success to-date to accelerate our growth tomorrow.

We seek business that will 1) Offer technology and/or services that are synergistic to our current product offering, 2) Compliment out existing operations, 3) Add strategic or competitive value to our operations and 4) Are profitable. Having the financial flexibility afforded as by the Shelf Registration is good financial housekeeping and allows us to act on an opportunity without delay at a time of our choosing and from a position of strength. This concludes my prepared remarks.

+++ q-and-a
Operator^ (Operator Instructions). We will be taking our first question from the line of Eric Stine from Craig-Hallum. Your line is open.

Eric Stine^ Hi, Bill and Dan, congrats on the ENGIE announcement this morning. Maybe just wanted to start with that, I mean, are there I know its early days but are there some next milestones that we should look for as part of this agreement. I guess, that would be part one and then part two, can you just talk about specific plans in France. I know in the past you've sized it that 2500 units, they'd be the full analyzer. So, any details on both of those would be great.

William Clough^ Yes. I think the next milestones as with any customer is get PO's, get the Purchase Order and we are in the process of negotiating that right now. So, they are moving forward in that regard. I still see that opportunity as we talked about in the past, they are a primarily high pressure operator, so we talking about the GasPTi, the integrated units which is the higher priced units.

And I still think the volumes are where we talked about less, a little less volume than you'll see in Italy but a larger priced item, obviously more than just the analyzer. The other end of it, though, is that I think it is a much broader much bigger potential customer than Snam Rete. I mean, it's a company that is huge in comparison. They run the entire energy grid in France as opposed to just a pipeline.

So, obviously we have opportunities in biomethane to grid, we have opportunities at the retail level, we have opportunities with the distribution level. This is a much larger opportunity and obviously from the press release, I think you got it from our comment, there is opportunities outside of France.

They have a huge presence in Asia, specifically in China with PetroChina and others and they are a big player in that regard and they are quite impressed with what we've done in their test lines. So, I'm quite excited about their relationship and think it's going to be a very big one.

Eric Stine^ Is there any way to think about size, I mean, obviously extremely large but when you talked about the six underground storage sites with PetroChina, I mean, any thoughts on number of GasPTi units or VE-probes that would be involved for one of those storage sites?

William Clough^ No. And I'd be guessing at this stage, I mean, really there's no way to quantify that opportunity, I mean, other than, we've always known that China was a huge opportunity. Our fear moving into Asia is always protection of our patents in of our proprietary information.

One that I see about this relationship is that we move in to that are of the world with a partner like ENGIE to that some extent protects us from what we might otherwise fear. Because they are so big, so respected, and so embedded there. So, but again I couldn't tell you the opportunity at this point. It's very early stages.

Eric Stine^ OK, fair enough. Maybe just turn into Snam Rete and still I mean any I know it's very difficult to predict, but are you noticing any progress in getting through some of the regulatory hurdles any way to think about potential timing that that's cleared up or is that up in the air at this point and when it happens their view is unchanged. You just don't know when it reengages?

William Clough^ And it would be difficult to say, there are not hurdles, [plural] hurdles, there is a hurdle.

Eric Stine^ OK.

William Clough^ It is a one issue hurdle which is to get through this regulatory tariff issue and they I can tell you having talked to them, they are moving as quickly as they can. They are, they've got a team of people who are dealing with the regulator, they've got a team of people who are writing the regulation, the tariff scheme, they've done this before, so they know how to do it.

They told me that they thought they would have it done by the end of last year that obviously didn't happen. So, they're telling me they're moving as quickly as they can and they have every intent of moving forward with the project as quickly as they can get it resolved. But I don't think anyone can really put a timeframe on it because again you're dealing with a very large slow moving bureaucracy.

On the other hand, I have received information that those units that have been installed would be quite effective. They're working 100% and they are showing what they expected. It's some relatively significant revenue increase, so I know they're quite motivated to go forward. But again, I can give you a date Eric, I would definitely give you that date, I just don't have it.

Eric Stine^ All right, right, no I get that, OK. Last one from me. Just you mentioned the Ofgem letter that is that something that is in consideration now, it sounds like that's something that you expect to get put in place in the somewhat near term?

William Clough Yes. We expect that the issue any day now, actually. We were told that it was going to come out at the beginning of this week and we didn't get it. But we expected any time now. We've been expecting now for a couple of weeks. They closed the commentary on January 6th and told us that we have something by the end of February and obviously that hasn't happened either. But again, we're back dealing with regulators. But I do expect something any day. And we will not make a secret of it. And that will be once we hear about it, we'll put it out.

Eric Stine^ OK. Thanks a lot.

William Clough^ Sure. Thanks, Eric.

Operator^ Thank you. Our next question comes from the line of Joe Maxa from Dougherty & Company. Your line is open.

Joe Maxa^ Talking more about the Ofgem letter, once that comes out, can you give us a little color on the regulatory process and what it has to go through and perhaps how long that might take realistically?

William Clough^ Now, the regulatory, the issue the real issue is the regulation. The regulation is it is this is the process. We've gone through extensive testing behind the scenes. So, Joe we've gone through extensive testing behind the scenes with Ofgem and a testing facility that they have. We've done all of that. The letter, the comment letter is the last phase of that. They put that out as I mentioned close that comment period on January 6th.

The next step is the regulation. There will be a regulation able issue. And at that point we become applicable across the board to all of their off-take sites small and large and more importantly to the biomethane to grid application. Which means we can, I mean, it's a real basic thing. We can undercut anyone else in that field, by as much as a GBP150,000. Well, that makes us really the leaders in the industry.

There'll be, it'll be very difficult for anybody to could be with us on a bidding basis for those types of devices.

Joe Maxa^ So, how quickly before you would expect to see some revenue once this happens?

William Clough^ I think there are bids in place right now that we would be able to revise and lower that we could get almost immediately. You would see projects awarded very quick, I mean, in a matter of weeks.

Joe Maxa^ OK. That sounds very promising. Back on the ENGIE piece of it. Have they committed to using your GasPT both on their network and their these biomethane to grid systems?

William Clough^ Yes. We're negotiated right now to develop and decide on the size of the project. They're absolutely committed. In fact, I said in front of them one of the nicest things that happened during the course of negotiation sitting in front of them in

Paris, is when an issue came up from one of the subsidiaries that well we have to do some durability and accuracy testing and their lead engineer, lead test engineer stopped him and said "No, we've done that, we know the device works, we know it's durable, we know it's accurate. That's not necessary.

So, again I think we have accomplished what we wanted in Western Europe. We finally have the major player in Western Europe, in essence adopting or accepting the accuracy and durability and yes I think we're going to have some nice news over the next short period of time. We have -- they are definitely committed to the technology. They're very green gas oriented. They're very efficiency oriented, and they really are looking to rollout a large number of both the biomethane skids -- the bio-methane-to-gas skids rather, and the devices across their network.

Joe Maxa^ Right. And Dan, one for you. So, the gross margins were lower than typical both segments, or than they've been in a while. A little more color on that, please, and what are you looking for as we move forward?

Daniel Ford^ Sure. The gas margin was lower really because we had just a few GasPT's in the quarter compared to the previous quarter. And the GasPT's really, the GasPT's and VE's really drive up margin in the energy segment. When the energy segment is more based on projects, large project skids, those kind of things, the margins are more in the mid-30s range. So, that's why the energy segment margin was down.

We are looking for that margin to stay up around the high-30s to low-40s percent for the short term, and as Snam Rete picks back, we'll expect to see in the 40s again. Or if when ENGIE ramps up their project as well, we would expect that to happen.

The power and electric mechanical side is still in a competitive time where we are being impacted by lower margins out of the Canadian facility products just due to continued work to get that fully ramped up. It is improving, but that will impact the margins there. We are also seeing a turnaround the last several months in our distribution sales are beginning to pick up; our distribution sales are where we do fairly well with the margin -- a lot because it has the product mix that customer to achieve good pricing on that and good margins versus higher volume direct sales usually have mid 30s to high 30s margin, but we can sell as distribution we can do very well in that business. So as the distribution network picks up -- sales activity, that’s improving as well. The power segment margins head back up into the high 30s this year.

Joe Maxa^ OK. That's helpful. And lastly, backlog is down a little bit sequentially. So would we be looking at Q1 being similar to Q4? And then, how would you frame the year, Bill, going forward -- I mean, just kind of a pick-up each quarter type as more and more of these projects start getting accepted? And you’ve obviously announced a lot of positive opportunities coming, just wanted to see what you are thinking about how the year progresses?

William Clough^ Yes. We think that the first quarter is going to be similar to fourth quarter, which we were fairly up-front about that we thought that would be soft. We do now see strengthening as the quarter has continued. We had some fairly nice announcements, and we will continue to have nice announcements. We think that both segments on a core basis are growing, are beginning to grow again. We think the electronics division will be high single-digit growth this year, and we think the energy division just on its core business will also be growing.

The X factors are obviously Snam Rete when the picks up, ENGIE and how quick they can gear up, and then in the power and electromechanical areas, the ICE Block technology, we have several units out in field trials. They are doing quite well, and that's another end of the industry that could pick up. So again I think we are -- we still see this as a growth year, and we think that as the quarters develop, we will see sequential growth quarter-over-quarter.

Operator^ Thank you. Our next question comes from Rob Brown from Lake Street Capital Markets. Your line is open.

Rob Brown^ Morning, Bill. Could you maybe characterize the ENGIE roll-out, kind of the structure, what's your sense and how they roll-out? Do they do it over multiple-years? Is it, I guess what's the roll-out?

William Clough^ Sure. I would tell you that what we announced this morning was a collaboration agreement so the roll-out is going to be over many years. They are actually looking to partner with us. They are taking us to their customers as a partner. As part of their new technology portfolio. So they are bringing us in as a partner with them. So it's more than just a customer-, if you will, vendor relationship but it's a much closer than that.

Now as to individual roll-out I think that we have already been introduced and are currently negotiating with their integration unit which is the company called ENDE. ENDEL is the one that does all their infrastructure work inside France -- and those are the ones who will be building and deploying these biomethane to grid skids that is going to be used in the green gas area. They have taught us about significant project in that regard. That project is a multi-year project to roll-out as many as a thousand of these skids and they will include our GasPT technology and more importantly I think our expertise in that type of deployment again it is a multi-year situation where we will see that over the course of several years five or more.

The same thing with movement into their network. The network is a project that they think about in terms of 5, 10, 15, 20 years out they are very progressive. They are very forward thinking but again we are early days right now negotiating this so as far as specific timing it’s hard to say -- we are already talking in -- so we are already talking about the –biomethane to grid skids. So if that answers your question.

Rob Brown^ That's great. Thank you. That helps and then on Italy how many units I know you delivered I guess how many you delivered, how many are actually installed and operating at this point?

William Clough^ Yes. We delivered 400 I don't know the exact numbers [on installations] because they are not sharing that. They have been installing though. We finished deliveries in October of last year and they have been installing small numbers, I can't tell you how many.

But there are a number of units installed and I know that because they have told me the results on those units but again, I couldn't put a number on it. I can tell you though that they are very, very committed to the project and have told us they are all geared up and ready to go back to 100 units a month of installation.

One of the reasons they have been installing even though they haven't yet resolved this piece is because they have used the tier one installation company to get themselves ready so they know they can install them quickly and efficiently. They have got commissioning process setup with their distributor Socrates and they have done that on a number of occasions to make sure that everything is set and goes. So they are ready to do 100 a month as soon as they get this resolved, but I do not have a number an exact number of what they have installed.

Rob Brown^ OK. Thank you. I will turn over.

Operator^ (Operator Instruction). And we are taking our next question from the line of Amit Dayal from Rodman & Renshaw.

Amit Dayal^ Thank you. Good morning, Bill. Good morning, Dan. Congrats on the ENGIE agreement.

Just in that context, we saw sort of larger framework agreement with National Grid and given that we have so many touch points sales touch points with ENGIE could we see some of the similar agreement [to National Grid] potentially with ENGIE as well?

William Clough^ Absolutely. I think that's something we will be working towards frankly. Again as I mentioned this is early stages. We just signed this collaboration agreement. We are meeting with them. I have a team meeting with them on a weekly basis so we are exploring all sorts of alternatives and what we can do to help them. They are really seeing in a big way, the multiple applications of these technologies if they can really control the grid and monitor that entire grid they can much more actively deliver gas and they think obviously obtain more revenues from the same gas. That's their key all over Europe. But again we think that's a very strong potential.

The difference being as I mentioned is unlike National Grid that really operates just the high pressure pipeline, ENGIE operates the entire energy network for France and it's so much bigger operation.

Amit Dayal^ Understood. Thank you for that. And then just in relation to the biomethane opportunity could you give us some context in terms of how large this market is potentially for you?

William Clough^ Yes. It depends on the geographic area. We are probably reaching the tipping point with the U. K. where there won't be a whole lot more I think maybe we have 17 sorry I think we have three in process. So we will have 20 out there and I think honestly there is probably no more than 35 or 40 that are going to be done and there are other vendors.

In the case of France, they are talking about a thousand units. In the case of U. S. certainly at one point when the EPA was talking about expansive biomethane to grid solution there is as many as 11,000 potential intake points in the U. S. We don't think that will be quite as large simply because new administration has less emphasis on alternative energy. However, we do have seven bids out in North America right now. Several in California. And I think two or three in Canada. So we do have bids out there.

Again but it's really geographically based and it depends obviously on the altitude, the political environment to those geographies. In Europe green gas, bio-gas is very, very popular. In fact as you may know many of the countries have set up a program where they expect to get 20% of their energy from alternative sources by 2018, 2019 so there is a big push there so it really depends geographically but it is a large opportunity.

Amit Dayal^ Understood. You mentioned in your commentary potential acquisition I mean has there been something identified that you may pursue in the near term?

William Clough^ We have several specific targets that we are looking frankly none of which I would identify publicly because we are again early stages but we are always looking and we feel that there are things available now certainly the North American energy market that would be synergistic, profitable and would fit with our product portfolio. So there are several areas that we are looking.

Amit Dayal^ And maybe just one last one from higher strategic perspective as well I guess, from a product development point of view both for the CUI Global part of the business and CUI Inc. are there any new offerings that we are looking to launch in 2017?

William Clough^ Yes. I think one of the things we touched on earlier and I think it's something that we are really working towards now is along with the collaboration agreement we are now talking to ENGIE about very unique and differentiated method of odorizing the gas. It's a micro-odorizer that we think could be quite industry shift when it comes to odorization of gas. So there are products that we are looking at and of course the electromechanical area this ICE BLOCK technology could be a huge play for us simply because it is such -- it has such broad application across the blade server market. So we are always looking for new technologies that we can launch.

Amit Dayal^ Awesome. Thank you so much guys.

Operator^ Thank you. Our next question comes from the line of Joe Maxa from Dougherty & Company. Your line is open.

Joe Maxa^ Yes. Hi, Bill. A follow-up on the potential acquisitions, maybe a little bit more color on what you are looking for?

I mean is it more product specific to fit into your existing channel? Or you are looking for more of a distribution geographic presences hopefully little color and then also what multiples are you seeing or you willing to pay for potential acquisitions?

William Clough^ Yes. The multiples -- that's a difficult question to answer. It really depends on what the Company is I mean we are seeing everything from four times EBITDA to as much as ten, 12 times EBITDA depending on what is it that we are looking at. We are looking at primarily, the companies that we would be looking at are number one companies that are not broken; that are profitable; that are in fact making money that have management team in place, that are working and then working well.

We don't want to go in and try fix something. That's something that we are not looking for at all. In regards the type of companies we are really looking in the energy market, that's what we are looking and we are looking for companies that either expand our product base or expand our customer base or preferably do both.

So we would be looking at companies that are involved in metering, involved in analysis, involved in really doing what we do know which is the monitoring and metering of the gas pipeline system. That means we are looking at companies that provide meters, provide applications that we don't have and then expand us into customers that we don't have. So that's what we are looking. Expanded product, expanded customer and again profitability that's really where we headed for.

Joe Maxa^ Thank you.

Operator^ Ladies and gentlemen, that's all the time that we have for questions this morning. So I would like to turn the call back over to the management team for closing comments.

William Clough^ Thanks, Andrew. I appreciate -- thank you everybody for your time and attention and obviously for your patience and your support of the Company. We feel that this is going to be a very transformational year in many different ways and we obviously are available to you if you need to talk to us. We again thank you for your support and thank you for your time. Thank you, Andrew.

Operator^ Thank you. Ladies and gentlemen this now concludes today's program. Thank you again for your participation. You may now disconnect.