Operator: Greetings and welcome to the Transcat First Quarter Fiscal Year 2018 Financial Results Conference Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. As a reminder, this conference is being recorded.

I would now like to turn the conference over to your host, Mr. Craig Mychajluk. Thank you, sir. You may begin.

Craig Mychajluk: Yes, thank you, and good morning, everyone. We certainly appreciate your time today and interest in Transcat. With me here on the call, we have Transcat's President and CEO, Lee Rudow, and our Chief Financial Officer, Mike Tschiderer. After formal remarks, we will open up the call for questions.

If you don't have the news release that crossed the wire after markets closed yesterday, it can be found on our website at transcat.com. The slides that accompany today's discussion are also on our website. If you would, please refer to Slide 2. As you are aware, we may make forward-looking statements during the formal presentation and Q&A portion of this teleconference. Those statements apply to future events, which are subject to risks and uncertainties, as well as other factors that could cause the actual results to differ materially from where we are today. These factors are outlined in the news release, as well as with documents filed by the company with the Securities and Exchange Commission. You can find those on our website, where we regularly post information about the company, as well as on the SEC's website at sec.gov. We undertake no obligation to publicly update or correct any of the forward-looking statements contained in this call, whether as a result of new information, future events or otherwise, except as required by law. Please review our forward-looking statements in conjunction with these precautionary factors.

I would like to point out as well that, during today's call, we will discuss certain non-GAAP measures, which we believe will be useful in evaluating our performance. You should not consider the presentation of this additional information in isolation or as a substitute for results prepared in accordance with GAAP. We have provided reconciliations of non-GAAP to comparable GAAP measures in the tables accompanying the earnings release.

With that, I will turn the call over to Lee to begin the discussion. Lee?

Lee Rudow: Okay. Thank you, Craig. Good morning, everyone, and thank you for joining us on the call today. We will follow the same format as we have in the past. I will hit upon some highlights for the quarter and then Michael will provide more in-depth review of the financials before I wrap things up with an outlook for the year. So, it was a good start generally to fiscal 2018 as we generated $36.3 million of consolidated revenue, which represents a 9.4% increase. The quarter saw solid growth in both our service and distribution segments. With our last acquisition, Excalibur, being a year old at the start of the fiscal year, all the growth in the first quarter was organic.

Let's start with the Service segment. In the first quarter, the Service segment delivered strong organic growth of 7.6%. This is the consolidated Service growth rate, which includes Canada. Our U.S. Service organic growth rate was about 9%. We have now achieved 33 consecutive quarters of year-over-year Service growth. That's an accomplishment we are very proud of. Demand through the quarter was strong and we continue to take market share. In fact, we are seeing strong revenue growth into second quarter as well.

In addition to growing our targeted life science market during the quarter, we gained quite a bit of traction in defense and high-end electronics as well. As we mentioned in the news release, we ramped up new labor resources that we expect will position us well for the rest of the year. Of course, productivity for new technicians is low at first, so we managed the volume. The volume increased by increasing technicians over time. It is not a bad challenge to have and the

one we see leveling out and correcting itself. It's important to note that we do not have a physical capacity issue. It's basically on the technician's side and that's where we are focusing some of our attention.

The only other thing I would add in terms of color for the Service segment in the quarter is that we invested $1.2 million of capital for new service capabilities, which is a bit higher than what we normally spend in the first quarter, but it was in response to new opportunities and demand. We expect the utilization of the investments to increase throughout the year as they get fully deployed. We still expect to be within our $6 million to $6.5 million CapEx forecast for the fiscal year.

Moving on to Distribution, segment sales were strong with improved growth and operating margin. Sales for the quarter were up 11.4% as we saw U.S. core industrial markets strengthen, including some recovery in oil and gas. Our rental business continues to perform well and grow at an impressive rate. I'd also add that, from a marketing perspective, we love the work that our technology team is doing. We have generated significant gains in our domain authority and associated web traffic, both of which had led to higher quoting levels, calibration sales on new product and lead generation for our service segment.

With that, let me turn things over to Mike to discuss the results and I will come back and talk about our outlook.

Mike Tschiderer: Thanks, Lee, and good morning, everyone. I will be referring to the presentation slides that complement our earnings release. As mentioned, both are available on EDGAR and on our website.

Starting on Slide 4 of the deck, we show our top line revenue performance by segment and on a consolidated basis. We have provided a little color on the drivers of each segment. And as a final reminder, this quarter's growth for both segments was all organic as our last acquisition, Excalibur, was right at the beginning of our fiscal year 2017. We expect our Service segment to achieve double-digit sales growth over time from a combination of organic and acquisitive growth. We are very pleased with the 7.6% organic growth performance in the first quarter. This is in line with our goal of mid to high single-digit organic growth.

As noted on the slide, the Service segment continues to deliver strong results over the long-term, with mid-teen growth over both a trailing 12-month period and CAGR since fiscal 2014. Our Distribution business continued its strong momentum, increasing revenue 11.4% in the quarter. This growth was a direct reflection of our diversification strategy, as well as an improving U.S. industrial market. Additionally, the Excalibur acquisition brought us a network of independent sales representatives who are currently focused on selling new and used equipment and equipment rentals. Early results have been favorable, especially with new equipment sales. Additionally, order bookings have been strong early into our second quarter.

Moving on to Slide 5, quarterly consolidated operating income was impacted by the investments made in the quarter, the technician labor capacity Lee discussed and $322,000 of a one-off stock-based compensation expense recorded in the quarter non-cash. As a result, operating income was consistent quarter-over-quarter and operating margin declined 40 basis points to 3.9%. The stock-based comp expense was split almost 50:50 between our two segments. This negatively impacted operating margin by 90 basis points in both the Service and Distribution segments.

Our total operating expenses were 20.1% of consolidated revenue in the first quarter of fiscal 2018 compared with 20.5% of consolidated revenue in the first quarter of fiscal 2017. We expect to see our Service segment margins improve as sales begin to flow through our new and existing calibration capabilities and as the productivity of newly hired technicians improves. On the Distribution side, our gross margin increased from higher margin equipment rentals and

used equipment sales, along with increased volume based vendor rebates, which when combined with cost controls resulted in segment operating margins spanning 50 basis points.

On Slide 6, we show adjusted EBITDA and adjusted EBITDA margins. Among other measures, we use adjusted EBITDA, which is a non-GAAP measure, to gauge performance of our service and distribution segments, because we believe it is a good measure of operating performance and is used by investors and others to evaluate and compare performance of core operations from period to period. I do encourage you to look at the reconciliation of adjusted EBITDA to the closest GAAP measures for us (operating income and net income) that we have provided. Quarterly adjusted EBITDA increased more than 8% to $3.4 million and was driven by strong growth in the distribution segment, which increased more than 50% to $1.1 million. As a percent of revenue, consolidated adjusted EBITDA margin was down nominally 10 basis points to 9.3%.

On Slide 7, first quarter net income was $860,000, down just slightly over the first quarter of fiscal 2017 as a lower effective income tax rate nearly offset slightly increased interest costs. The effective tax rate for the first quarter was lower than typical at 24.8%, largely due to the discrete tax benefit recorded from accounting for certain stock based compensation awards. We still expect our effective tax rate to range between 34% and 36% for full year fiscal 2018.

Slide 8 provides detail regarding our balance sheet and our cash flow, which support our growth strategy. During the quarter, which typically is not a strong generating quarter for cash, we used $2.9 million of net cash in operations. This higher than typical usage stems from the timing of working capital changes, especially the timing of certain vendor payments and the payout of prior year bonus and profit sharing awards during the quarter. We fully expect to generate cash from operations for the remainder of the year. Our total capital expenditures were $2.1 million for the quarter and were primarily for customer driven opportunities to support our Service capabilities and for assets to support our growing rental business. Of note, we have made investments into our mobile calibration fleet. For those of you that may not know, we have built a fleet of mobile calibration trailers that can provide service at customer sites, which may not have the space or the utility capabilities we require to service their equipment. This mobile capacity is especially valued in the alternative energy sector. During the quarter, we also added reference level radio frequency and microwave calibration capabilities in our Houston, Texas calibration service center.

Total CapEx is still planned to be approximately $6 million to $6.5 million in the full year fiscal ’18, with the remaining expenditures focused on other Service-related capabilities, as well as on IT infrastructure investments to drive our operational excellence initiatives. Of the CapEx plan for fiscal 2018, approximately $1 million to $1.5 million of the $6 million to $6.5 million is for maintenance or existing asset replacements.

At quarter end, we had total debt of $32 million, with $6.4 million available under our revolving credit facility. Debt was temporary elevated during the quarter, up $4.6 million since fiscal year 2017 year end, given the timing of capital investments and the usage of cash in operations. Despite that, our leverage ratio is still relatively low at 2.2x, a ratio we are comfortable with, especially considering the timing of working capital changes that will level out over the remainder of the year. We calculate our leverage ratio as total debt on the balance sheet at quarter end divided by trailing 12 months adjusted EBITDA; other companies may calculate such a metric differently.

We believe we continue to have sufficient liquidity and ample dry powder for any investment opportunities or acquisitions that meet our strategic criteria. Lastly, we expected to timely file our Form 10-Q on or around August 4.

With that I will turn it back to Lee.

Lee Rudow: Okay. Thank you, Mike. So, the first quarter of fiscal '18 is in the books. Our strategy and focus have not changed and we are pleased with the prospects of both operating segments. Recently, we spent a lot of time talking about operational excellence and initiative is well underway. Over time, we expect operational excellence to support strong sustainable organic growth and margin enhancement. Goals include process improvements across the business from acquisition integration to order processing. The ultimate goal is to leverage technology and processes of a competitive advantage for Transcat. It won't happen overnight, but the process has started. It's an important one and it's getting a lot of attention and focus. As we progress through fiscal '18, we expect the Service segment to continue to deliver mid to high single-digit organic growth. The increasing demand that started in the fourth quarter of last year continued in the first quarter and second quarter as well. Our new business pipeline is strong; it continues to provide nice momentum.

From a labor perspective, we are making progress on increasing our capacity. Like I said before, it's a nice challenge to have and we are working through it. We made a significant number of early year investments to strategically increase our service capabilities and we expect increased utilization of the investments throughout the year and into next year. Distribution has performed well and we will continue to be pleased with the impact the rental and used equipment businesses had on the segment, both directly through higher margin profile and indirectly through the enhancement of our value proposition across our Service segment and the entire organization. Furthermore, we have said and demonstrated in the past that acquisitions will remain an integral part of our growth strategy and, from a pipeline perspective, we are in a good position. That said, most recently, we have been focused on organic growth investments and what has been a productive and responsive market. So, overall, we expect a strong fiscal 2018. Looking further out, we are tracking well to reach our sales target of $175 million to $200 million over the next 2 years to 3 years.

So with that, I will turn things over to the operator for any questions.

Operator: Thank you. At this time, we will be conducting the question-and-answer session. Our first question comes from the line of Bill Sutherland of The Benchmark Company. Please proceed with your question.

Bill Sutherland: Good morning. Thanks for taking the question. I was really impressed with Distribution growth. Just curious, as you look at that quarter and then, obviously, going forward, how much do you feel that the pickup is, the backdrop tailwind versus some of the things you are doing just to grab share?

Lee Rudow: Bill, this is Lee. I think it's a combination. I mentioned it in the script and walked you through some of the notes. We have done a really nice job with some of our web presence, our domain authority. We are getting a ton of leads relative to what we have produced in the past or the last couple of years. It has really been building over time, some of the momentum and some of the work that we put into lead generations, so I think that's part of it. I would certainly credit the group here for producing that benefit. I think there is a bit of a tailwind as well, so I guess that it's a combination. Certainly, relative to oil and gas, we have seen some recovery and, when I say some recovery, I think it bottomed out if you will. There is price and some pent-up demand. Some of our vendors, with instruments that particularly relate to oil and gas and the transmission of signals along that process, have seen an up-tick in business and we have seen it as well. So it's a blend. I wouldn't put a percentage on it. I like the work we are doing. I think it's had a big impact. It's nice to operate in an environment that doesn't have headwind. I think you are seeing some of what this company can produce in at least a neutral environment; there will be a little help from the macros.

Bill Sutherland: And then, in Services, the labor constraints only impacted gross margin, not growth, is that correct?

Mike Tschiderer: A little bit of both. I will start off with, at least, that it didn't impact the revenue growth even though we continue to have a good, we call it, work in progress of backlog and work on the shelves that would be done in July. What we saw was the cost of getting the work out was higher, because of the mix of overtime versus having fully trained up staff, which gets to the hiring and recruiting and training programs that are going on.

Lee Rudow: Right, but, with a consistent buildup of back orders, had we had the staff here early enough and trained up quickly enough, I think you are seeing some revenue increase as well, so I agree with Mike; it's really a combination. There would have been higher levels of growth in combination with some margin without any question that the margins would have improved.

Bill Sutherland: Did the order flow tick-up in a way that you were somewhat surprised in terms of the number of techs that you had?

Lee Rudow: That's a great question. I would say that we were probably a little bit late in recognizing that this was starting in the Q4 of last year. We probably could have gotten ahead a little bit, but since we have recognized it, we started ramping up. In this business, it's not always easy to turn on a dime. We have had a significant number of technicians do a really nice internal recruiting program that we started in Q4 that produced a lot of labor. In Q1, we are just going to get the productivity up. We didn't necessarily see this volume pickup, but we knew that we were improving each quarter on organic growth. It's really picked up the momentum. We are really happy to see it.

Bill Sutherland: And these positions, Lee, you can't use contract type employees, can you?

Lee Rudow: No, not really. With these employees, even if they're experienced in the industry, it takes a good month or two months to get experience on our systems, so that's part of it. I don't see this as a long-term issue, but when you look quarter-to-quarter and you get an up-tick in the business, you are going to see quarters like this. We will flatten out and level out over the year.

Bill Sutherland: So, that was my last question actually, the ramp of the new tech. It's not several months; it sounds like it's…?

Lee Rudow: No, I will give it a quarter or so and we will be well positioned. We have had organic growth at least in the U.S. of almost 9%. If that goes to something significantly higher, we can end up in the same position later in the year and that would be a nice problem to have too. I think we are in a good position for the current volume.

Bill Sutherland: On the M&A pipeline, you are saying it's fairly active, but it's not the priority it's been in past years at this point?

Lee Rudow: I am not sure I would characterize it that way. What I would say is that a couple of years ago, 12 months or 24 months back, when the macros were more challenging, what that sometimes provides Bill is an environment. It's really nice for making good acquisition deals. So, what we try to do here when we allocate resources is try to do so and be well aware of the opportunities that we have. Sometimes you have more opportunities. It's a better opportunity to make an acquisition and sometimes organic growth is really strong. We think organic growth has been pretty consistent for the last year or so and really responses, so I would say that what you are going to see moving forward is a blend of both. We have a nice pipeline. We have made a lot of acquisitions. We have done well with integrating them and finding them and paying the right price. We are very disciplined and we are going to remain disciplined. I just want to note that, in the last year, we have invested more time and energy and money into organic growth, because the market was so responsive. I wouldn't read into that. We can't do both at the same time, because we always have and I would expect that to continue into the future.

Bill Sutherland: Okay. Last one for me is on Distribution and you call this out in your filings about the increased competition from platforms like Amazon and those kinds of more consumer level distribution. What are you doing - and it doesn't seem like it's a source of pressure on your Distribution numbers - and how do you position yourself going forward against that kind of competition?

Lee Rudow: I think the key is the overall comprehensive strength of our value proposition. When you look at Transcat today, I don't look at it as Distribution, I look at it as the combination of Distribution, with the elements of rentals and used and stock house, and our Service business. If somebody wants to order not just one unit or two units, but 50 units in a variety of vendors, we still are a very viable option. If these units need to be calibrated upfront with uncertainty data and performance data, we have a very strong value proposition. And with our Service customers, Bill, across the country, they regularly buy instruments from us, because of the combined relationship we have on both our Service and Distribution segments. I look at Transcat's strength and some of the momentum we have had in Distribution, some of it is rentals, some of it is used, some of it is combined value proposition of the whole company. That's where we are uniquely positioned. We don't know of another company in the country that, if you look at the key elements of our value proposition, which include Distribution, Service and the elements of each, present the market the type of you proposition that we do. So I think that combined strength and, as long as we are not having significant headwinds, you are going to see some better performance and that's what we are seeing now.

Bill Sutherland: Yes, definitely. Thanks again for taking the questions.

Lee Rudow: Okay, good question. Thank you.

Operator: Our next question comes from Dean Trudeau, a private investor. Please proceed with your question.

Dean Trudeau: Most of my questions were answered, so I just have one. Is there a certain amount of leverage where you start to become uncomfortable? You mentioned that there is still stuff in the acquisition pipeline or the M&A pipeline potentially. You are sitting pretty low at 2.2x, but maybe you could just give me some context on that?

Lee Rudow: Yes, sure. Thanks, Dean. We are very comfortable, especially with the timing of the 2.2x, which we think is high right now as EBITDA grows and some of the working capital things adjust out, but we are still comfortable with something and I'd go higher into the twos. We are not comfortable with anything nor would our bank be comfortable at something into the 3x trailing 12 months, but we believe that we have enough there and it's still a good time to be borrowing and we are comfortable at 2.2x, even though we think that will go down, ex any acquisitions or any other unusual activity.

Dean Trudeau: Okay, great. Thanks.

Lee Rudow: Thanks, Dean.

Operator: Our next question comes from Steven Stern of Stern Investment Advisory. Please proceed with your question.

Steven Stern: Thank you and good morning everyone. My question concerns the Distribution segment sales. What is the breakdown of that number between rentals and outright sales on a percentage basis?

Mike Tschiderer: Yes. We don't disclose rentals as a number or as a separate segment. If it continues to grow, we probably will, but as a rough range, of our Distribution of over $70 million, our rental is still $2 million to $3 million of revenue. It's still very small, Steven, compared with

the total Distribution segment revenue. It's a more compelling and it brings more to the bottom line just because the profitability margin is different than a core distribution product. Eventually, if it continues to grow like we hope it will, we could see it as a separate reportable segment, but it's in that range.

Steven Stern: Okay. What are the rentals or leases or what type of time period…?

Lee Rudow: Yes. It ranges anywhere from weeks to we have had some that are 2 years. I will say probably the sweet spot is in that 4-week to 12-week period. The business that we got from Excalibur, their rental business, which is typically higher-cost, higher-end electronic gear, is typically a little bit longer average rental period than a Transcat, which is more of a meter-based, a smaller dollar piece of equipment. We are talking 6 weeks to 18 weeks for an Excalibur, sometimes up to six months.

Operator: There are no further questions. I would like to turn the call back to management for closing remarks.

Lee Rudow: Okay. Well, thank you for joining us on the call today. We appreciate your continued interest in Transcat. Feel free to reach out to us at any time. We look forward to talking to you all again after our second quarter results are released. For those who are going to be in the Chicago area, we will be presenting and holding investor meetings at the IDEAS Conference at the end of August. Again, thank you for participating and have a nice day.

Operator: This concludes today's conference. You may disconnect your lines at this time. Thank you for your participation and have a wonderful day.