



Profire Energy, Inc.

Fourth Quarter 2021 Earnings Call

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PRESENTATION

Operator

Good morning everyone, and thank you for participating in today's conference call to discuss Profire Energy's Fourth Quarter and Full Year 2021 ended December 31, 2021.

I will now turn the call over to Steven Hooser, Investor Relations at Three Part Advisors to get the call started.

Steven Hooser

Thank you Operator. With me on the call today is Co-CEO and CFO of Profire Energy, Ryan Oviatt, and Co-CEO Cameron Tidball.

Before we begin today's call, I would like to take a moment to read the Company's Safe Harbor statement. Statements made during this call that are not historic are forward-looking statements. This call contains forward-looking statements including but not limited to statements regarding the Company's expected growth, impact of higher oil prices, management of the supply chain and anticipated impacts of government sanctions, expansions in new markets, customer adoption of the PF2200 product line, investments in the launch of new products, anticipated sales opportunities and planned projects, the

ability of the Company's resources to make beneficial investments in 2022 and beyond, the Company's exploration of M&A opportunities and the Company's future financial performance.

All such forward-looking statements are subject to uncertainties and changes in circumstances. Forward-looking statements are not guarantees of future results or performance and involve risks, assumptions and uncertainties that could cause actual events or results to differ materially from the events or results described in or anticipated by the forward-looking statements. Factors that could materially affect such forward-looking statements include certain economic, business, public market and regulatory risk factors identified in the Company's periodic reports filed with the Securities and Exchange Commission. All forward-looking statements are made pursuant to the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995. All forward-looking statements are made only as of the date of the release and the Company assumes no obligation to update forward-looking statements to reflect subsequent events or circumstances, except as required by law. Readers should not place undue reliance on these forward-looking statements.

I would like to remind everyone that this call is being recorded and will be available for a replay through March 23, 2022 starting later this evening. It will be accessible via a link provided in yesterday's press release as well as the Company's website at www.profireenergy.com. Following the remarks by Mr. Oviatt and Tidball, we will open the call for questions.

Now I'd like to turn the call over to Co-CEO and CFO of Profire Energy, Mr. Ryan Oviatt. Ryan?

Ryan Oviatt

Thank you Steven, and welcome to all of you who are joining us on the call today. I will start the call by providing some updates on our industry and our business followed by a review of the financial results, and then I will turn the call over to Cam to discuss the quarter's highlights, outlook and strategic direction.

Our 2021 results reflect the gradual recovery of the economy following the extended global shutdowns in 2020. Revenue, gross profit and EBITDA increased sequentially each quarter during the year in line with oil demand increases and oil price improvements driven largely by the reopening of economies worldwide. Subsequent to year end, oil prices have risen and topped \$120 per barrel for the first time since 2008. This is putting increased pressure on U.S. and Canadian producers to begin ramping up production, however we expect the near term impact to be modest as producers grapple with the challenges of finding the additional skilled labor and available drilling and production equipment necessary to achieve higher production volumes. The lack of capital spending over the past two years will be a challenge for producers and will likely limit their ability to scale quickly.

Thankfully, the COVID case rates have started to decrease dramatically in the U.S. and most places around the world. This has caused the CDC along with many additional state and local governments to roll back mask mandates for indoor environments, and a number of companies are beginning to set dates for employees to return to work in the office. We are part of this trend and are excited that our Canadian employees can once again gather in our facility as a full team, like our U.S. workforce has been able to do for some time now.

The EIA expects global production to meet or slightly exceed demand later this year, but the current geopolitical climate may result in greater volatility in prices and global inventory levels. This adds to the already challenged environment resulting from lower production levels over the past two years. The recent unrest in Ukraine has contributed to the upward pressure on oil prices. Until yesterday, the Biden administration had not sanctioned Russian oil exports which represents approximately 8% of U.S. oil imports. If these sanctions were to be combined with fewer government restrictions on U.S. oil production, this could have a significant impact on our business and the U.S. oil industry in general.

With that, let me shift gears and turn my remarks to Profire's financial results for the fourth quarter and full year 2021.

Yesterday after the market closed, we filed our Form 10-K with the SEC and discussed the quarter and full year highlights in a press release. As always, both of those documents are available on the Investors section of our website. The transcript of this call will be posted in the coming days.

In the fourth quarter, we recognized \$8.3 million in revenue, which represents a 19% increase over Q3 and a 47% increase over the prior year quarter. The sequential and year-over-year increases are primarily due to the continued economic recovery from the COVID-19 pandemic. Gross profit increased to \$3.4 million as compared to \$3.1 million in the third quarter of 2021 and \$2.8 million in the year ago quarter. Gross margin decreased sequentially to 41.6% of revenues from 44.9% due primarily to product and customer mix. In an effort to help combat the unprecedented inflationary pressures experienced throughout 2021, we implemented a price increase across our product line at the end of 2021.

Total operating expenses for the fourth quarter were approximately \$3.7 million compared to \$3.4 million in the third quarter and \$2.8 million in the fourth quarter of 2020. The sequential and year-over-year increases reflect the significant cost inflation impact on our business combined with re-staffing efforts in response to the recovery during the year. Specifically, G&A expenses for the fourth quarter increased 8% sequentially and 36% year-over-year. R&D expense decreased 7% on a sequential basis but increased 20% from the prior year quarter. Depreciation and amortization increased 58% sequentially and 55% as compared to the same quarter a year ago.

Net loss for the fourth quarter was approximately \$145,000 or breakeven on a per-share basis. This compares to net income of \$92,000 or breakeven on a diluted share basis in the third quarter of 2021, and net income of \$56,000 or breakeven per diluted share in the fourth quarter of last year.

Cash flow from operations in the fourth quarter was a negative \$309,000 compared to a positive \$142,000 in the prior year quarter. During the quarter, we repurchased approximately 664,000 shares of our common stock for approximately \$755,000. As of December 31, 2021, we had roughly \$1.2 million remaining on our repurchase program.

For the full year 2021, we recognized \$26.4 million in revenue. This compares to \$21.5 million in 2020. The 23% increase is primarily due to the increased customer demand related to the ongoing economic recovery from the pandemic as well as our success and progress in the strategic growth segments of our business. Gross profit increased to \$11.4 million as compared to \$9.5 million in the prior year. Gross margin decreased to 43.3% of revenues from 44.4% in the prior year. This year-over-year decrease in gross margin is primarily due to product and service mix and inflationary pressures on both fixed and variable costs.

Total operating expenses for the year were approximately \$13.4 million. This represents an \$810,000 increase from 2020. The increase is primarily related to higher G&A expenses resulting from overall cost inflation and the re-staffing of positions correlated to the recovery of our business; however, this 6% increase was lower than our revenue growth rate for the year. R&D expense decreased 14% and depreciation and amortization increased 14% compared to the prior year.

Total other income during the year was \$334,000 compared to \$421,000 last year. The decrease is attributable to fewer fixed asset sales and the associated gains or losses year over year.

Net loss for the year was approximately \$1.1 million or \$0.02 per share. This compares to a net loss of \$2.2 million or \$0.05 per share last year.

Cash flow from operations for the full year was \$649,000 and our cash and other investments totaled \$17.5 million compared to \$17.6 million at the end of 2020. We had no borrowings or other debt on the balance sheet at year end.

Capital expenditures for the year were approximately \$169,000.

Our inventory balance at the end of the year was approximately \$7.2 million, down from \$8.4 million at the end of 2020. To date, we have been able to adequately meet our level of customer demand; however, continued disruption of the supply chain over the next three to six months could make this more challenging. We will continue to proactively work with our suppliers to procure the necessary parts and components to deliver our BMS solution while replenishing the inventory used over the past couple years.

I will now turn the call over to Cam to provide an overview of our business. Cam?

Cameron Tidball

Thank you Ryan. We are excited about the financial results for the fourth quarter. In the quarter, we were able to achieve the highest top line revenue for a single quarter since Q3 of 2019. We are encouraged by the positive trends that are supporting improvements in both our core legacy business as well as our diversification efforts into new industries.

Looking at our core legacy business, the combined onshore rig count for the U.S. and Canada averaged 704 in the quarter, representing an 11% increase from the previous quarter, as well as an 80% increase from the beginning of the fiscal year. The average WTI price per barrel of oil in Q4 was \$77, representing a 10% increase from the previous quarter. Producers continue to draw down on previously drilled but uncompleted wells as the DUC count decreased to 4,650 at the end of 2021, representing a 48% drop from its peak in June of 2020.

We have and continue to see positive signs from our customers, such as increased drilling activity and plans for additional equipment upgrades. We are encouraged by recent industry consolidation activity which has new buyers looking to modernize the assets they have acquired. These signs will likely create additional opportunities with both new and existing customers. Although Profire has prepared for these expected increases, we are also dealing with challenging supply chain issues and human capital constraints that are impacting most industries.

Our sales team continues to find new and expanded opportunities for our PF3100 platform. We continue to gain momentum in selling to customers who have larger, more complex burner applications. We expect that our solutions, project execution including engineering and design, price point and product performance set us apart from traditional competition at larger midstream plant operations and facilities. This has led to increased quoting and proposal activity that we believe will support our 2022 revenue goals and targets; however, we may see some revenue volatility quarter over quarter as we navigate the industry supply chain challenges.

The PF2200 continues to roll out successfully. Approximately half of our customer base has begun adopting the PF2200 platform. Some early adopters have already begun to spec the PF2200 as their base platform. We expect the majority of our customers to shift over their new equipment purchases to the PF2200 between now and the end of 2023.

We remain focused on finding opportunities to expand our solutions offerings to our existing customers. Emissions monitoring and quantification continues to dominate the press and in turn the minds of our customers. We feel our existing customer relationships present a strong opportunity for Profire to bring

these types of solutions to our customers through potential partnerships, acquisitions, or other investments. We are investing in R&D to bring additional solutions that we believe will help our customers in their efforts to track, measure and quantify emissions and support their efforts to demonstrate that they are producing responsibly sourced gas.

In the fourth quarter of 2021, we received repeat orders or completed new combustion projects in biogas, power generation, landfill, water and wastewater, chemical, construction and infrastructure, and food and beverage. Projects completed in the fiscal year in the mining, renewable, and biogas industries were focused specifically on efficiency improvements and the destruction of fugitive emissions, including methane and other VOCs. We continue to strengthen our pipeline for non-oil and gas project opportunities and we expect to see meaningful growth in this area in 2022 and beyond. We continue to develop relationships with existing and potential strategic partners, end users and OEMs from the industries mentioned above and the quantity of opportunities continues to trend upward.

In the quarter, we received purchase orders for products and services to support a new dryer appliance in a food and beverage processing plant of a leading national supplement manufacturer. We expect there will be opportunities to upgrade the existing heated appliances at this same facility in the future. We were also awarded a significant upgrade project at an LNG fractionation facility which we expect will be executed in the second quarter of this year.

In response to the ongoing positive signs and use cases for our combustion products and expertise in alternative industries, we have added an additional resource to our sales team. We now have two full-time sales representatives focused exclusively on these initiatives outside of oil and gas. We have also restructured our compensation strategy for key team members, including business leaders and sales team members to promote business development efforts focused on this strategic initiative.

In 2021, we were successful in our push for business growth in midstream oil and gas as we completed several significant projects at larger midstream operations. Our successes are enabling us to pursue repeat business and to credibly approach other midstream plants with large multi-burner applications with a proven track record. We continue to invest time and energy in investigation of potential acquisitions which are complementary to our vision and growth initiatives. As always, this is a challenging and time consuming process. Profire will continue to employ proper due diligence to balance risk versus reward in assessing these opportunities.

As we reflect on the previous year, we look forward with optimism in 2022 and beyond. Looking at the future of our business, we feel that we are in a better position to capitalize on the organic growth from our core business and to execute on our growth strategy into new industries. We have expanded and have successfully proven the value of a larger suite of burner management solutions, including controllers, high efficiency burners, and service exposure. Our customer base continues to expand and our sales and service team continues to assist our customers with critical safety and efficiency solutions.

Our sales pipelines in our legacy business, midstream plant operations, and non-oil and gas industries continue to strength. We have added to our sales team as our market has expanded, supporting our strategy to enter new industries. We continue to work on development of existing and new strategic sales and distribution partnerships specifically with those who have high exposure to applications found in non-oil and gas industries. Stability of oil and gas prices at or above current EIA forecasts should enable our extensive customer base to invest further in technology upgrades as well as expand drilling and completion plans.

We have continued to manage our cash position effectively. Through our share repurchase program, we have repurchased 664,000 shares of 1.4% of total outstanding shares prior to starting the program.

Before we turn to questions, Ryan and I would like to once again thank our employees for their continued dedication and commitment to the ongoing success of Profire, our customers, and our shareholders.

Operator, would you please provide the appropriate instructions so we can get the Q&A started?

Operator

Thank you.

Our first question comes from the line of Rob Brown with Lake Street Capital Markets. Please proceed with your question.

Cameron Tidball

Good morning Rob.

Rob Brown

Good morning guys. First on the environment, obviously a lot has changed over the last few weeks. What are you seeing in terms of the customer demand environment more into this year, and how do you--you know, historically does higher oil prices sort of flow through to you in terms of timing?

Cameron Tidball

I can definitely tackle that one here first, Rob. Thanks for the question.

If you look at—obviously it's not really an elephant in the room, but the developments in Russia and Ukraine, we've got a lot of questions over the last few days, months, weeks about what will this mean. Really, they've obviously ignited, pardon the pun, but our core market, which is really already a coiled spring, if you look at what our customers, we knew as early as in the middle of Q4, we expected, we forecasted that we would see an increase in production. It just had to happen with the decrease of DUCs, the fact that there's 50% less from its peak, that's a huge issue for U.S. shale when it comes down to it, because not all of those DUCs are completion worthy, so we already knew there had to be some increase in production. We're seeing the COVID numbers go down, so we expected this, an increase to occur in 2022. Obviously we saw a nice uptick in 2021 in the fourth quarter and the back half of the year, as we predicted, but with the whole Russia-Ukraine thing, if you're alluding to that, and maybe you're not, that's going to take time really for the U.S., and even North America gas and oil producers to catch up. It's really a six-month thing before they could even add those incremental barrels that will be a deficit from Russia being out of this.

We still think that things are positive for our industry. The oil prices being up doesn't hurt, that's for sure - it definitely helps us, and it will flow through to us eventually, but as Ryan mentioned in his comments, there is a lag on that for sure.

Ryan, did you want to add anything to that?

Ryan Oviatt

Yes, I'll just comment a little bit on oil prices and your comments. Historically if we look back prior to three, four years ago, higher oil prices pretty quickly translated into increased drilling programs in the U.S. and Canada. We're in a completely different environment now, and lots of different pressures, regulatory pressure and even global macro pressures as well, to where we're not likely to see that happening. But

even back then what that happened, it would be a quick ramp-up on rig count or on drilling, but then it was a three to six-month lag for us when they actually needed the production equipment to go onto those new wells. So, that cycle is still accurate and it'd still apply, maybe shortened somewhat because of new technology, but in the current environment, as you can see, the E&Ps here in the U.S. are holding back and they're not making the moves because of the government pressure, the additional regulations and restrictions that have been placed on the industry.

As I mentioned in my previous comments, I think we really have to see a softening of some of those pressures from the White House, from the administration before we're going to start to see a significant ramp-up, and that might mean some pain for people at the pump and in other ways for a little bit longer, until we can really see that change happen.

Rob Brown

Okay, great. Thank you for that color.

Then also on the--and I think you were specifically talking about the non-oil and gas projects, the pipeline of projects ramping up you alluded to, could you kind of give us a sense of how many projects are in the pipeline, maybe the size of the revenue opportunity there over the next couple years?

Cameron Tidball

That's always fun to forecast. What we can share is yes, we've definitely seen some success - we've now got the two sales team members rocking on it, but we're also empowered our team members who service more of that upstream, midstream and downstream transmission business to look for those opportunities. We have a project team in house that supports these, as well as those larger projects that go into the downstream side of midstream, but as we look at what this looks like, as we mentioned in the comments just earlier here, we saw meaningful growth from \$21 million to \$26 million, and there was not a substantial but a meaningful percentage of that increase was due to the efforts outside of oil and gas.

So what does that pipeline look like, what are the number of projects in the pipeline? It's larger than it ever has been. We had a good year last year overall in terms of revenue in that space. We don't see it in the next two years being 50% of our revenue, but we do think that it could eventually be in the next couple years to a point where there would be more reason to bring on more sales team members. We'll continue to add and look for strategic partners, potentially acquisitions that are complementary to those efforts of expanding, keeping true to our core business of combustion and technology solutions related to that.

So, no real numbers to give you there yet, Rob, but we hope that in the future, we're able to more fully substantiate it with numbers.

Ryan Oviatt

I'll just add to that, it's not only the outside of oil and gas new industries that Cam was talking about there, but we did see a meaningful increase in our growth segments within oil and gas, so that bottom half of midstream and refining petrochemical, we're seeing a lot of progress in those areas as well. Those are some of those projects where we've been able to now go back with a track record of saying, look, we've done this, it's very similar to what you've got, and we're getting more quoting and winning more projects in those areas as well within oil and gas, but also that outside of oil and gas diversification.

Rob Brown

Great, thank you. I'll turn it over.

Ryan Oviatt

Thanks Rob.

Operator

Thank you. Our next question comes from the line of Jim McIlree with Dawson James. Please proceed with your question.

Cameron Tidball

Hello Jim.

Jim McIlree

Yes, thank you. Good morning.

Ryan, you talked about—or maybe it was Cam, you talked about a price increase at the beginning of the year. Could you quantify that or put a range around how big the price increase was?

Ryan Oviatt

Yes, so I mentioned it, but I'll let Cam talk about the size and its overall—our approach to it and how it's functioning for us.

Cameron Tidball

Yes, as we looked at the price increase, we knew we needed to do it, and we implemented it late Q4. We gave our customers a little bit of time as they prepared their budgets for 2022. We obviously saw somewhat of an influx, a small influx of orders coming in because people wanting to get ahead of the price increase to a degree, which we monitored, we didn't let anybody to play any dirty tricks, but for the most part our customers accepted it.

The range, approximately 10%. Obviously on some of the proprietary products that Profire has, we were able to go a little higher, and some of the resale products we're not able to go as high. We more wait for what our—our vendors raise their prices, we'll raise our prices in accordance with them. But we also had to consider just obviously our increases to the bottom line of Profire of moving these prices up. It was well overdue, it was the right time, but we had to be very conscious of the fact that we still are in a somewhat very competitive market when it comes to upstream and midstream burner management. Yes, we're the dominant player, we've always been the more expensive product because we provide a better solution than our competitors, but we couldn't go to a point of pushing customers to looking at alternatives because, as much as the barrel is high overnight and the last few weeks, it wasn't that high in December, and it's not likely to sustain at this. It's going to go all over the place, it's very volatile, but we feel like we put in an increase that will support Profire's ability to get back into the black and to be a breakeven and profitable company, which is the goal. But we also have to wait and see how this all plays out. We've heard some vendors are increasing by 5, some to 15, some to 20. We thought that that average of 10% was the right mix for us.

Ryan Oviatt

We're going to continue to monitor that--you know, in the coming year at least, if not beyond as far as the inflationary impacts on our business, on our costs and labor and everything, and if we need to make additional adjustments in 2022, then we will do that, and maybe it's multiple times. It's not necessarily the scenario we want because it means our costs are rising as well, but it's certainly something that we will continue to pay close attention to.

Jim McIlree

All right, thanks for that. The gross margin decline in Q4 relative to Q3, it seems like it's bigger than a mix issue. Is there anything else going on there, or was there something special about the orders or the mix that accounted for the relatively large quarter-to-quarter decline in gross margin?

Ryan Oviatt

Yes, unfortunately it was a bit larger than we have typically seen, but it is a combination of those factors. Obviously some inflation was coming into play there. As Cam mentioned and as we just discussed, the sales price increase didn't really happen until the end of the quarter, so that didn't help benefit or offset those inflationary pressures. But, we did see a tremendous ramp-up in sales at the end of the quarter as well, and it turned out that a lot of those sales were from customers, larger customers, OEMs and others in that similar scenario where they do garner a little bit of a discount on our typical sales price, so that's where the customer mix and even product mix came in. The contribution from service is much lower and service revenue coming into play as well, being strong during that period, so it's really a combination of those factors, but we did see a significant increase in customer orders from the larger customer base, where they do have a little bit of a higher discount than some of the smaller customers.

Cam, anything else you want to add on that sales-customer mix?

Cameron Tidball

No, you captured it well. Definitely the larger OEMs and resellers that are working with the bigger producers, our mix of going direct versus through that channel in the quarter was definitely different than historical, so you captured it well.

Jim McIlree

Great. Ryan, you referred a couple of times to regulatory actions that could help increase production. Can you be a little bit more specific on what you're referring to?

Ryan Oviatt

Well, if we look back to what the Biden administration did in their first weeks and month in their office, they obviously cut construction on the Keystone pipeline. I think renewing that, reopening that would provide additional alternatives to oil supply here in the U.S., bringing in oil from Canada and Alaska, so that would be one key thing.

But then also, the restrictions that they've put on new leases, obviously there's still lots of lease—undrilled lease land out there available that producers have, but in an environment like this where the administration continues to speak towards longer term goals of significant reductions in fossil fuel production and use in the U.S., I think the E&P executives and leadership teams, owners are struggling to see why they would want to make significant expensive investments in drilling programs and infrastructure in things that are going to cost them a ton of money, but in the long term perspective, at

least what this administration is pushing for, are not likely to have that long term payoff or that long term payback.

It's the restrictions they've actually put in place, I know there are restrictions on new LNG facilities in the U.S. as well that are being held up, so there are lots of different areas where this is impacting the industry, but it's also that overall tone and message that's telling E&P companies to hold back on very expensive, massive improvements until they can see a time where those returns are going to be more profitable for them in the long term. My personal view, of course, but I think there's a lot of evidence out there that supports that.

Jim McIlree

All right, that's great. Thanks a lot, guys, and we'll speak soon.

Cameron Tidball

Thanks Jim.

Ryan Oviatt

Excellent, thanks Jim.

Operator

Thank you. Our next question comes from the line of John White with ROTH Capital Partners. Please proceed with your question.

John White

Good morning guys.

Cameron Tidball

Hey John.

John White

Yes, congratulations, nice results. Nice to see the revenue improvement.

Back to the price increase, was that pretty much across the board? It sounds like it was.

Ryan Oviatt

Yes, for the most part we—there was some corrections on—you know, we went through a massive pricing project, actually, and for a company our size to do that, what a lift by the team to go through it from one, from analysis, two to implementation with currency differences both in vendors and in customers, discount levels. It's quite an undertaking and we wish it was just you pushed a button in our ERP and it did it, but it doesn't so it was quite a lift. But yes, on average that 10% is pretty much across the board, almost every product has moved on average, and again some we'll do better on and some we'll do as good, and some we'll do a little bit less. But for the most part—we really targeted obviously kind of that 80% to 90% of the products that make up our revenue. That was the target focus of the project.

John White

Okay, thanks. You mentioned business benefiting from exploration and production mergers and consolidation. Can you give us some examples or talk more about that?

Cameron Tidball

For sure. Obviously there was—I think it was Cabot and Cimarex. It's not like we were—we look at these and go, wow, that end user wasn't using us, the other one who bought them is, and then we get it, although we've benefited from that in the past. But what we like to see if obviously 2021 reports have—merger and acquisition and activity was as high as its been for quite a while. I can't remember the quantification of the dollars, but it was huge, especially compared to the previous two years.

What we see from this, what we like about it is there's still companies, obviously there's sellers and there's buyers. It'd be worrisome if there was a ton of sellers and no one buying, but we're seeing that consolidation which we believe means more push towards automation solutions, which we believe pushes more towards autonomous production, which lends to, one, our existing product suite, it lends to safety, as you get these bigger E&Ps, they have bigger and better safety programs. They are also more conscious of, of course, ESG initiatives, especially around the emissions side of things, and so we just see that as a good opportunity for Profire.

It does create work for the sales and administration teams of Profire and service teams, as we have to cut things over, we have to learn new billing systems, we've got to make new contacts, we've got to see who shakes out in all the shuffle, but overall, we see it as a positive thing because these companies that are doing this, they're not looking to buy assets to just let them die. They're looking to buy strong assets to bring them into the fleet, the connect them and to gain production from them. There'd be no other reason for it, in our opinion, so it's a very positive thing, we think, for Profire.

John White

That all makes sense, and I appreciate the extra detail. I'll pass it on.

Cameron Tidball

Thanks John.

Ryan Oviatt

Thanks John.

Operator

Thank you.

Our next question comes from the line of John Bair with Ascend Wealth Advisors. Please proceed with your question.

John Bair

Thank you, and good morning. I kind of want to circle back a little bit to the margin aspect. Just saying, okay, so you've had a number of your larger customers, you got some bump in order flow in the fourth quarter when that was announced, so the question is do you anticipate your overall margin profile will

improve as we go through this year with those price increases, and I guess specifically, how do you feel you can improve those margins so that you become more profitable with the expanding base?

Ryan Oviatt

Yes, good questions John, and absolutely we believe that the sales price bump will help with that. It's a very key reason as to why we're doing it. How much is it going to benefit, we can't necessarily quantify that just yet, but if we're bringing up prices on average 10%, hopefully it's having that amount of impact to offset costs certainly for us in that regard, so we do absolutely expect that that's going to help. As I mentioned before, we'll continue to monitor our overall cost inflation side as well to make sure that it's not continuing to outpace the sales adjustment we have made, and if we need to, we'll continue to make others in order to try to keep that margin improvement happening.

Then as we look at the pipeline of projects that we talked about earlier as well, a lot of those projects come with improved margins themselves, just because of the nature of the projects. They tend to be a lot bigger, there is a lot more work involved on the engineering, design, implementation, actually installation, all of that that goes along with those, so we certainly are maintaining good solid margins on these bigger projects, and as we are expanding into other industries, so far we're seeing that the margins are holding in those areas. But as we've made adjustments over the last two years to our cost structure, we certainly downsized or right-sized the business to get through COVID and now we're coming back out of COVID, but we didn't completely cut everything to where we could still have those same margins and net margins at \$20 million in revenue or at \$25 million in revenue. We still believe this is coming out of the bottom and that we're getting back up, and that the future for Profire isn't at \$25 million to \$30 million annual revenue business, but is much bigger than that.

We're still building that structure and maintaining the structure that we believe we need to capitalize on these significant increases that could be coming here in the near future, and therefore we've got the structure, we believe, that will help support that. As we go through that growth and we ramp back up, we certainly expect that margins are going to benefit from higher revenue and lower fixed—not lower fixed costs, but not having to grow fixed costs as quickly as we do grow revenue.

John Bair

Okay, and hopefully you get more of the newer projects with better margins in them, and that should provide a boost there. Is that a fair way of looking at it?

Ryan Oviatt

Yes, absolutely. Cam, any other thoughts on your end or comments as far as those projects go in the pipeline and their impact on margin?

Cameron Tidball

No, you covered it well. As it becomes a bigger part of our business, these other projects, the downstream side of midstream, as we've talked about, and outside oil and gas, just diversification initiatives, if we can maintain or on some of them get higher, there will be some where it will be up and down, but on average it should be able to maintain more around those historical margins.

John Bair

Okay, and then outside of the price increases and so forth, how are you addressing any raw material cost or component cost pressures that you're experiencing right now?

Ryan Oviatt

Absolutely we—sorry, go ahead, Cam.

Cameron Tidball

Yes, I was just going to say I'll give it to Ryan, but that's why we moved the call to so early in the morning, because we don't sleep anymore. That's all we do, is worry about that.

No, Ryan, you speak to it.

John Bair

I just figured you were doing a deal out east, that's all.

Ryan Oviatt

Yes, we're doing the best that we can. We've got a great team that's monitoring our components and materials, that's looking at alternatives and other options when we're seeing significant increases. Cam jokes, but within—for Cam and I and even for that team, it is long hours and it's a significant effort right now to try and maintain the supply and get the stuff that we have already ordered in a timely fashion, but then also try to keep costs down as much as we can and, like I said, look for other alternative sources or options without destroying or disrupting the quality that we maintain for our products and our services. It's a significant effort and we're going to continue to put that in.

John Bair

Is building inventory part of that process of certain things that you can get faster than others?

Ryan Oviatt

Yes, absolutely. We historically have maintained a high level of inventory, that's come down over the last couple of years, but we're focused on rebuilding that and even maybe bringing on more inventory as quickly as we can to meet what we see as significant demand coming this year and at least into the following year.

John Bair

Okay, very good. Some of my other questions I had have been addressed earlier, appreciate it. Good luck going forward. Encouraging.

Ryan Oviatt

Thanks John.

Operator

Thank you. Our next question comes from the line of Arie Coll with Coll Capital. Please proceed with your question.

Arie Coll

Good morning gentlemen, thank you for taking my question. First question just is about inventory. You ended the quarter here with—the December quarter with \$7.2 million of inventory. Can you give us an update for how long it is taking for you to procure all the various parts you need to build up inventory, and are there any specific parts where there's kind of a real shortage, where there is maybe a six-month lag time or something, and those specific parts could make it difficult to produce finished goods?

Ryan Oviatt

Yes, certainly. We have a wide mix of inventory and components, a lot of those components going into our systems to build a finished complete BMS system. We've got all the peripheral parts that then build a complete BMS solution, so the flame arresters, the burners, all of these different things we've kept in inventory. From a systems perspective, it's an area where we're probably seeing the most challenge right now, and it's not every component within the system but it's often ones or twos in components that have grown in significant lead time, so we're seeing a lot of components in the 6-month to 12-month lead time and moving in that direction. We've been working very hard to try and get orders in and deal and manage with those lead times.

Cam, any more specific comments on the components or our inventory process there?

Cameron Tidball

Yes, when you look at Profire has historically held substantial inventories and it's been a strategy of ours, and we're going to continue to work towards, it's one of our value propositions to our customers, is that we have inventory on hand. But as we look at some of these components are, as you mentioned Arieh. like six months, some have even to a point—some vendors have come out and said we're canceling order—we're not canceling orders, we're canceling delivery dates because we don't know, we don't have anything to give you. They're tired of picking up the phone from our procurement team, is what it really is.

But what we were pleased to see, not that but the fact that we were able to pivot in our strategy over the years to have, wherever possible, multiple vendors to supply products so that we can shift and pivot quickly. We've done some great things to avoid some really complicated situations to a degree, and we've talked about it. We're almost to a degree lucky that U.S. shale cannot respond as quick as they would like to or potentially would want to, especially if regulatory pressures would allow them to expand production to fill this gap of the—what would it be, like 700,000 barrels a day, there'd be nobody could keep up. But we've seen, again, these issues from vendors, but our team has done a great job in the past to prepare for and to just pivot quickly.

As Ryan mentioned, it's single components, it's not massive component lists for each part, but you look at our bill of materials for our systems, for example, it's a very long and complicated list of parts coming from many different places, which is part of our strategic advantage. But the team has done a great job to pivot as quick as possible to find new suppliers, new replacement parts, certification updates, etc.

Arieh Coll

Yes, let me just ask the question again. I mean, there's certain industries, like let's say the automobile industry, where there's specific semiconductors that are just not available and so cars can't be produced. I'm trying to understand to what degree—how challenging is it for you to get the components you need, because in some industries, yes there's a shortage, but if you pay 20% more, the components you need will be available, and so what I'm trying to understand is in the spectrum—I mean, if your orders went up substantially, would you be—what I'm saying is, if your inventory, let's say today, was depleted, would

you be able to get all the components you need even by paying higher prices, or are there certain parts where they're just not available and you need to wait six months for them?

Cameron Tidball

Yes, this is interesting because I was talking to one of our team members and drove by one of the larger dealerships here near the shop here in Alberta, Canada, and there was seven Ford pickups on the lot - seven. There's nothing--they're in a place where, yes, they cannot get anything. We would have a mix of that. Luckily we do—we planned ahead, for example for our systems, we've had some of the core, key components that are long lead times and that we saw future end of life on, for example our PF2100 platform where we have ample stock, where we—but we would have a mix of that. I wouldn't be able to pinpoint that it was all or nothing for any of them, and some of them, they're just longer lead times, but some of them you can't pay more, they're just not there. For example, our solenoid manufacturers, our valves, if they're not there, they're not there. But for the most part we're ahead of these things, but it is still a shuffling struggle to make sure we have the right things for the right orders at the right time.

I don't know if that answers it for you perfectly. There isn't a perfect answer. We've got a mix of both.

Arieh Coll

Okay, and then just more clearly on the inflation that you've had in your cost of goods, what's your weighted average increase in your cost of goods that's taken place that's resulted in the decline here in gross margin that was reported?

Ryan Oviatt

That's not really a number that I can quantify or provide. We're seeing it all in labor. We're seeing it in the cost of our contract manufacturers as we're talking about all of these different components, each of the components are having increases that are coming through to us, and then on our side, the cost of labor to complete the solutions, do the assemblies in our facilities, those things have been going up fairly significantly. I think labor increases overall are in the probably 10% to 12% increase range across the business over the last 12 to 18 months, so as far as giving you a specific increase, I can't do it, but we're seeing those inflationary pressures in every aspect of the business from our utilities to labor to raw materials components, just like every other business is.

Arieh Coll

Got it, okay. Listen - best of luck in being able to provide the goods your customers need. It sounds like you're very well positioned because if you look at your inventory, it's the equivalent of about six months of sales at the current run rate, so it's not as if you're down to your last two BMS systems by any stretch.

Ryan Oviatt

Yes, certainly. Again, appreciate your participation today, Arieh.

Arieh Coll

You're very welcome.

Operator

Thank you. Our next question comes from the line of James Jang with Univest. Please proceed with your question.

Ryan Oviatt

Hello James.

James Jang

Good morning Ryan, good morning Cam.

Cameron Tidball

Hey James.

James Jang

It was an interesting quarter, and I just have a couple of quick questions. One is you mentioned that you had an influx of orders near the end of the quarter, so are we to assume that those orders haven't been booked and those will flow through to the first quarter in terms of the top line?

Ryan Oviatt

No, actually we're saying those were booked in the quarter and that's what helped drive our revenue up to \$8.3 million for the quarter, and that's a significant increase over the prior quarter at \$6.9 million, so that's what we're saying, is we had that influx and they came in. But also in our comments about pipeline, that's more of the forward-looking, that the pipeline is building and for 2022, we're seeing all of those positive signs.

James Jang

Okay, great, and in terms of expansion into other sectors, have you been—I don't know if you can speak about this, but have you had inquiries from, I guess, smaller power plants, that what's being discussed now in the market is setting up small power plants at the source, at the wells, and then bringing on data centers and crypto miners there. Those mini projects that you seem to be involved, have you had any inquiries in that sector?

Cameron Tidball

We've been involved. There's one producer in particular who's been very active at that, and yes, our systems are being used there but I wouldn't quantify that as anything material so far that we've heard from expansion and that effort from small power gen to power gen sites on the pad - no, not yet.

James Jang

Got you, okay. With the price increases, do you expect any other further price increases this year?

Cameron Tidball

We look at it—as Ryan said, we're going to continue to monitor it. If we get an increase from vendors, we're going to pass that increase on, we have to. We hope to be able to keep our core product, Profire's product stable for—until probably look at it again—well, we'll be looking at it throughout the year, but into

that Q3, Q4. We don't want to be one of these customers, every three—or providers that does every three months; however, that being said, we've had to look at our truck rates and we'll have to look at whether it be surcharges or things like that. You look at to fill up a diesel right now it's, depending where you are, \$4 to \$6 a gallon for diesel, definitely no service provider budgeted for that last year, so we are already looking at things like that. Those will be more on the fly, but product mix—if it's not ours and we get an increase, we'll have to probably consider an increase. If it's ours, we hope to be able to go and just do a standard increase at the end of the year.

James Jang

Okay. The last question is the acquisitions you made back in '19, can you give us an update on how that has been working out?

Cameron Tidball

Yes, we mentioned in our comments, just having the ability to have a high performance burner, our sales—that's really why we bought the Millstream company, was to get their burner technology, air plate technology. It's definitely been a huge value for our customers. We're specced in—I couldn't even give you a number, but that is the primary burner we sell. We sell more burners than we've ever sold before, so that acquisition has worked good. Again, is it \$10 million? No, it's not, but for what we paid for it, basically an inventory purchase, we love the product, we love the ability to bring it to our customers.

The Midflow acquisition has been fantastic. The talent pool, the service expansion in the northeast, the support to our business development team and product development team, the relationship that was brought with ECI, meaning the Emerson Impact partner in the northeast, again they're in our top 20 for last year for customers plus they're starting to expand outside oil and gas as we had hoped, and we're seeing some opportunities come in the door, so very happy with those. They're fully integrated or they have been for a while, and we're looking for the next one that makes sense, for sure.

James Jang

Okay, and one last one here, I think it was Ryan that mentioned that with the Russian energy ban and the U.S. ramping up production, it'll still take about six months for the U.S. to kind of ramp up, if they so choose to. If that is the case, when do you expect to see more ordering activity come in? Would that be in the second quarter or could that bleed into the second half of the year?

Ryan Oviatt

I think it's certainly more likely for the second half of the year as far as significant changes in orders, because as we mentioned, there's a whole process. The drillers, the rigs have to become available to be able to ramp that up, so certainly costs and procurement of sand and fracking supplies and drilling and all of that's got to happen, and then at the same time they'll start to order the heaters and the treaters, the Amine re-boilers, all of those production pieces of equipment that need to be ordered, and we're a small piece of that. So, bringing those wells online is several months down the road, and then when they go online, that's when we come into play or our products come into play.

The longer term process for significant changes is pointing more towards a second half of the year; however, we are starting to see some increases now as well because of continued bringing down the DUC count and other activity that's already in place.

Cam, you sounded like you wanted to comment as well.

Cameron Tidball

Well, you covered it well. I guess there's two things here again, and I think I mentioned it earlier, the already predicted increase in activity for 2022 based on COVID, based on the DUC countdown, that has started for sure; but for the most part, we still think that, again, securing rigs, hiring the frac crews, locating equipment, drilling, completing wells, permitting - you know, that whole processing assuming permitting was in place, that was all—was that even ready for this year's (inaudible)? Probably not. For us we feel we were ready for the increase.

Now a Russia-Ukraine scenario increase, nobody is ready for that. Nobody can keep up to that, so I think, as Ryan mentioned, yes, even just the back half of this year to support what they were planning to do from almost the beginning of 2022, can't even bring in Ukraine and Russia into this, that's just going to make prices as volatile as they are right now. It is a tough scenario for E&Ps, even if they want to, and as much as Biden's getting criticism for going to Venezuela and maybe not looking to the neighbors up north or going to Iran, which I don't agree with that but I don't know that he has a choice, because U.S. shale cannot pick up this quick to fill the demand.

James Jang

Got you. Okay, understood. All right, well thank you for that. I'll pass onto somebody else now. Thanks.

Cameron Tidball

Thanks Jim.

Ryan Oviatt

Thanks James.

Operator

Thank you. Ladies and gentlemen, that concludes our question-and-answer session. I'll turn the floor back to Mr. Oviatt for any final comments.

Ryan Oviatt

Thanks everyone for joining us on our call today to discuss our fourth quarter and full year 2021 results. We'd like to thank all of you for your continued support. As always, we are available for any discussions or questions you may have. Also, we will be participating in the ROTH Capital Partners Conference next week and look forward to meeting with many of you there. Thank you and have a great day.

Operator

Thank you. This concludes today's conference. You may disconnect your lines at this time. Thank you for your participation.