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Voyant Americas

Comprehensive Analysis

Ameresco, Inc. (AMRC – $75.31) December 20, 2021*

Ameresco, Inc. (AMRC) provides energy efficiency and green energy services including facility energy infrastructure upgrades, renewable energy plant construction and operation, energy asset sales, and consulting services. Ameresco primarily sells its services to federal, state, and local governments through a direct sales force. Ameresco was founded in 2000 and is headquartered in Framingham, MA. Its fiscal year ends on 12/31.

Thesis Summary

We are concerned there may be elevated risk associated with the Southern California Edison (SCE) project given the project is the largest the Company has ever attempted and is required to be completed in a historically short timeframe. Our concerns are heightened given the Company indicated the SCE project was lower margin. Supply chain friction and a labor shortage heighten our concerns about SCE project timeline achievability. In our view, a fully contracted backlog (excluding SCE project backlog) decline highlights backlog quality deterioration and depressed backlog coverage (excluding the SCE project) highlights new order book and burn dependency. We are concerned elevated contract asset levels highlight potentially aggressive revenue recognition. In our view, depressed contract liability levels highlight lower upfront payment requirements, potentially aggressive revenue recognition, and/or may portend revenue pressure. Depressed cash flow levels and elevated insider selling heighten our earnings sustainability concerns. We are concerned the COVID-19 driven sales cycle extension and inflation may drive project delays and margin pressure. In our view, a non-Big Four auditor and an ongoing SEC investigation may highlight elevated accounting irregularity risk.

Catalysts and Timing

- Q4 21/FY 22 results/guidance are below expectations.
- Recent aggressive revenue recognition drives revenue pressure.
- Insider selling persists.
- The SCE project timeline is delayed and/or the SCE project pressures margins.

Company Data

Company Data	
Country/Exchange	US/NYSE
Shares Outstanding (mil)	33.6
Float (mil)	31.3
Short Interest (mil)	1.1
% of Float Short	3.4%
Average Volume (mil)	$23.4
52 Week Range	$37.70 – $101.86
Dividend Yield	0.0%
Market Cap (bil)	$4.0
Net Debt (bil)	$0.3
Enterprise Value (bil)	$4.3
FY 20 Rev (mil)/Rev Growth	$1,032.3 / 19.1%
FY 20 Adj. EBITDA (mil)	$117.9
FY 20 GM %/Change	18.1% / (80 bps)
FY 20 Adj. EBITDA Margin %/Chg	11.4% / 90 bps

Historical Earnings

	Actual	Expected	Surprise
Q3 21	$0.41	$0.34	22.4%
Q2 21	$0.34	$0.26	30.4%
Q1 21	$0.25	$0.09	167.9%

Estimate Drift

	EST	1M Ago	6M Ago	1YR Ago
Q4 21 Rev	$412.9	$412.9	$335.9	$321.2
FY 21 Rev	$1,211.6	$1,211.6	$1,142.1	$1,071.1
FY 22 Rev	$1,897.4	$1,897.4	$1,260.4	$1,192.5
Q4 21 EPS	$0.44	$0.44	$0.44	$0.43
FY 21 EPS	$1.43	$1.43	$1.27	$1.22
FY 22 EPS	$1.89	$1.89	$1.50	$1.45

Peers Mentioned In This Report

N/A

*** All research is completed as of 4:00PM – 4:15PM Eastern Time unless otherwise noted.**
Please refer to the end of this report for an updated version of *The Short List*.
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Background and Bull Story

Company Background

Company description: Ameresco, Inc. (AMRC) provides energy efficiency and green energy services including facility energy infrastructure upgrades, renewable energy plant construction and operation, energy asset sales, and consulting services. Ameresco primarily sells its services to federal, state, and local governments through a direct sales force. Ameresco was founded in 2000 and is headquartered in Framingham, MA. Its fiscal year ends on 12/31.

Results by segment: In FY 20, US Regions accounted for 38.8% (28.5%) of revenue (pretax income), US Federal accounted for 36.6% (46.1%), Canada accounted for 4.6% (2.6%), Non-Solar Distributed Generation accounted for 10.3% (13.5%), and all other accounted for 9.7% (9.2%). US Regions, US Federal, and Canada segment revenue include the design, engineering, and installation of equipment and other measures to improve a facility's energy infrastructure and renewable energy solutions, as well as services including Company-owned and customer plant development and operating and maintenance (O&M) services. Non-Solar Distributed Generation (DG) includes the sale of processed renewable gas fuel and electricity produced from renewable sources of energy other than solar and generated by the Company's owned plants, as well as O&M services for customer owned small-scale plants.

FY 20 Segment Analysis (as % of total)	Revenue	Pretax Income
US Regions	38.8%	28.5%
US Federal	36.6%	46.1%
Canada	4.6%	2.6%
Non-Solar DG	10.3%	13.5%
All other	9.7%	9.2%
Total	100.0%	100.0%

Revenue by type: In FY 20, project revenue accounted for 74.1% of revenue, energy assets accounted for 11.5%, O&M accounted for 7.0%, integrated-PV accounted for 3.8%, and other accounted for 3.7%. Project revenue relates to the construction of energy efficiency projects, which includes the design, engineering and installation of technologies to improve the energy efficiency and control the operation of a building's energy-and-waste-consuming systems. O&M revenue relates to ongoing operating and maintenance services provided under multi-year contracts after a project has been completed. Energy asset revenue is generated by the sale of electricity, heat, cooling, processed biogas, and renewable biomethane fuel from the Company's owned plants. Integrated-PV represents the sale of solar photovoltaic energy assets and the associated energy regulatory credits.

Revenue By Type Analysis (as % of revenue)	FY 20
Project revenue	74.1%
Energy assets	11.5%
O&M revenue	7.0%
Integrated-PV	3.8%
Other	3.7%
Total	100.0%

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Background on revenue recognition: In its FY 20 10K, the Company disclosed project revenue was recognized over-time using the cost-based input method (i.e. percentage of completion), O&M revenue was recognized on a straight-line over the contract term, and energy assets and integrated-PV revenue were recognized over-time as energy is delivered to the customer. The Company disclosed a "majority" of contracts had fixed price terms, but certain contracts had price protections (e.g. cost-plus). Revenue recognized in excess of billings is included in contract assets.

Background on customers and customer concentration: In FY 20, the US Federal government accounted for 36.6% of revenue and all other federal, state, provincial, or local governments accounted for 34.9%. Non-government customers accounted for 28.5% of revenue. In addition, the Company's largest 20 customers accounted for 62.4% of FY 20 revenue.

Customer Analysis (as % of revenue)	FY 20
US Federal government	36.6%
All other federal, state, provincial, or local governments	34.9%
Federal, state, provincial, or local governments	71.5%
Non-government customers	28.5%
Total	100.0%

Background on energy savings performance contracts: In its FY 20 10K, the Company disclosed it typically entered energy savings performance contracts (ESPC) for energy efficiency projects under which the Company guaranteed agreed-upon energy savings. Ameresco indicated a "significant amount" of government customer revenue was derived from ESPC contracts. The Company may be subject to certain penalties if agreed upon energy savings guarantees are not met. Ameresco enters three types of ESPCs: pre-agreed efficiency commitments, equipment level commitments, and a whole building-level commitment. Under a pre-agreed efficiency commitment, the customer reviews the project design and determines, upon completion of the project, whether the agreed upon energy efficiency performance has been met. Under an equipment level commitment, the Company commits to an energy efficiency improvement based on the difference between energy efficiency measured with new equipment compared to the old equipment. Under a whole building-level commitment, the Company commits to increased energy efficiency for a whole building as measured by the utility meter where usage is measured. Building-level commitment energy efficiency measurements may be required once, upon installation, based on an analysis of one or more sample installations, or repeated at agreed upon intervals generally over a period of up to 25 years.

Background on IDIQs: In its FY 20 10K, the Company disclosed most of the work it performed for the federal government was performed under indefinite life indefinite quantity agreements (IDIQ). IDIQ agreements allow the Company to enter contracts with agencies prior to establishing and agreeing on individual task orders.

Revenue by geography: In FY 20, the US accounted for 92.6% of revenue, Canada accounted for 4.4%, and all other accounted for 3.1%.

Geography Analysis (as % of revenue)	FY 20
US	92.6%
Canada	4.4%
All other	3.1%
Total	100.0%

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Seasonality: Over the past three years, Q3 (Q4) accounted for 26.0% (31.1%) of revenue on average. In its FY 20 10K, the Company represented government customers typically appropriated funds on their fiscal year (09/30) basis.

Seasonality Analysis (as % of total)	Q4	Q3	Q2	Q1
FY 20 quarterly revenue contribution	30.4%	27.4%	21.6%	20.6%
FY 19 quarterly revenue contribution	35.4%	24.5%	22.9%	17.3%
FY 18 quarterly revenue contribution	27.6%	26.1%	25.0%	21.3%
Three-year-average	31.1%	26.0%	23.2%	19.7%

Competition: In its FY 20 10K, Ameresco disclosed its core project construction/installation business competed with Constellation Energy Group, Energy Systems Group, Honeywell, Johnson Controls, NORESCO United Technologies, Schneider Electric, Siemens Building Technologies, and Trane Technologies. Ameresco disclosed its renewable energy plant business competed with many large power producers and renewable energy project developers. Ameresco disclosed its landfill gas (LFG) business competed primarily with large national project developers and landfill owners. Ameresco disclosed its Solar PV business competed with Borrego Solar, BlueWave Solar, Citizens Energy, Clean Energy Collective, Nexamp, SunPower Corp., Solect Energy, and Syncarpha Capital. Ameresco disclosed its O&M services business competed with EMCOR Energy Services, Comfort Systems USA, Honeywell, Johnson Controls, and Veolia.[1]

Bull Story: SCE, Green Energy, Customer Savings, Customer Mix, & Potential Acquisition

Southern California Edison project: On 10/21/21, Ameresco announced it entered into a contract with Southern California Edison (SCE) to design and build three grid scale battery energy storage systems. The Company represented the engineering, procurement, and construction price was approximately $892.0 million, and Ameresco was obligated to achieve substantial completion of the facilities no later than 08/01/22. On its Q3 21 Conference Call on 11/01/21, Company represented the contract was the largest in its history and it was working on "quite a few" similar, albeit smaller, deals with other energy providers as well. In its Q3 21 10Q, the Company indicated the SCE "significantly increased" fully contract backlog (we estimate project backlog would have been 37.7% higher including the SCE project).[2] In addition, Ameresco guided for the contract to be an "important driver" of results through FY 22.

Backlog Analysis	Q3 21
SCE project	$892.0
Project backlog (as reported)	$2,363.8
Backlog including SCE (Voyant estimate)	$3,255.8

Green energy trend/transition runway: In its Environmental, Social & Governance (ESG) Report on 03/29/21, the Company highlighted its owned renewable energy assets delivered a carbon reduction of 11.2 million metric tons of carbon dioxide, equivalent to more than 27,700.0 million passenger vehicle miles. In its Investor Presentation on 11/01/21, the Company highlighted it was enabling a low carbon future and ESG was "in its DNA." In its research

[1] Constellation Energy Group, Inc. (CEG), Energy Systems Group (private), Honeywell International, Inc. (HON), Johnson Controls International PLC (JCI), NORESCO United Technologies (private), Schneider Electric SE (SCHN.PA), Siemens Building Technologies (subsidiary of Siemens AG), Trane Technologies PLC (TT), Borrego Solar Systems (private), BlueWave Solar (private), Citizens Energy Group (private), Clean Energy Collective (subsidiary of North American Infrastructure Partners), Nexamp (private), SunPower Corporation (SPWR), Solect Energy (private), Syncarpha Capital (private), EMCOR Group, Inc. (EME), Comfort Systems USA, Inc. (FIX), and Veolia Environment SA (VIE.PA).
[2] Given the SCE project was awarded after Q3 21 period end, SCE project-related backlog was not included in disclosed Q3 21 backlog.

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report, "Future of Energy – Investing in Decarbonization," Morgan Stanley Market Research & Strategy guided for renewable energy's share of US utilities fuel to increase from 11.0% in CY 20 to 40.0% in CY 30.

> Last year, Ameresco's customer projects and owned renewable energy assets delivered a carbon reduction of approximately 11.2 million metric tons of carbon dioxide — equivalent to reducing greenhouse gas emissions from more than 27.7 billion miles driven by passenger vehicles. As a long-term trusted sustainability partner, we are committed to making a meaningful impact on a low carbon future and doing our part to ensure future generations will be able to enjoy this world to its fullest. (CEO Mr. George Sakellaris, Environmental, Social & Governance Report 2020, 03/29/21)

Customer cost savings drive demand: In its Investor Presentation on 11/01/21, the Company represented its Smart Energy Solutions reduced energy consumption and costs with capital projects and operational modifications. In addition, the Company represented ESPC contracts allowed customers to renew facilities with no upfront capital expenditure. Accordingly, the Company indicated the majority of projects were funded by energy cost savings and budget-neutral for the customer. On its Q3 21 Conference Call on 11/01/21, the Company highlighted budget-neutral cost savings a key selling point and significant demand driver.

> Several factors have started to come together that they are influencing customer decisions. For many customers, the attraction to budget neutral cost savings. (CEO Mr. George Sakellaris, Q3 21 Conference Call, 11/01/21)

Potential acquisition risk: In an interview with Power Magazine on 06/02/20, CEO Mr. George Sakellaris represented he sold NORESCO, the first energy services company in the US, before launching Ameresco in 2000.[3] In its Proxy Statement on 04/27/21, Ameresco disclosed CEO Mr. George Sakellaris held a 6.9% interest in Ameresco and maintained 74.8% of the total voting power through class B shares. In its FY 20 10K, Ameresco disclosed CEO Mr. George Sakellaris was 74 years old as of 02/26/21. Given (1) Ameresco's CEO sold a similar energy service company in the past, (2) maintains majority voting control of Ameresco, and (3) is 74 years old, we believe there may be risk Ameresco is acquired.

Valuation: On 11/01/21, Ameresco reported Q3 21 revenue (non-GAAP earnings) of $273.7 million ($0.41), 10.1% below (22.4% above) the consensus estimate. While we acknowledge Ameresco is a pure play green/renewable energy Company and certain peers may have other business lines, as of the date of this publication, Ameresco shares traded at 40.1 times next-twelve-month earnings expectations, 96.3% above the peer group average.

[3] https://www.powermag.com/the-power-interview-amerescos-ceo-on-efficiency-renewables-and-resilience/

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Valuation Analysis	NTM P/E
Ameresco, Inc. (AMRC)	40.1x
Comfort Systems USA, Inc. (FIX)	20.6x
EMCOR Group, Inc. (EME)	15.8x
Emerson Electric (EMR)	18.2x
Johnson Controls International PLC (JCI)	22.6x
Trane Technologies PLC (TT)	28.1x
Siemens Ltd. (SIEMau.NS)	17.4x
Peer average	20.4x
AMRC above (below) peer average	*96.3%*

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Voyant's Earnings Risk Assessment

We are concerned there may be elevated risk associated with the Southern California Edison (SCE) project given the project is the largest the Company has ever attempted and is required to be completed in a historically short timeframe. Our concerns are heightened given the Company indicated the SCE project was lower margin. Supply chain friction and a labor shortage heighten our concerns about SCE project timeline achievability. In our view, a fully contracted backlog (excluding SCE project backlog) decline highlights backlog quality deterioration and depressed backlog coverage (excluding the SCE project) highlights new order book and burn dependency. We are concerned elevated contract asset levels highlight potentially aggressive revenue recognition. In our view, depressed contract liability levels highlight lower upfront payment requirements, potentially aggressive revenue recognition, and/or may portend revenue pressure. Depressed cash flow levels and elevated insider selling heighten our earnings sustainability concerns. We are concerned the COVID-19 driven sales cycle extension and inflation may drive project delays and margin pressure. In our view, a non-Big Four auditor and an ongoing SEC investigation may highlight elevated accounting irregularity risk.

SCE Deal May Present Unique Challenges And Margin Risk, In Our View

Background on SCE deal: As mentioned, on 10/21/21, the Company announced it entered into an $892.0 million engineering, procurement, and construction contract, the largest deal in its history, with Southern California Edison (SCE) for the installation of three grid scale battery energy storage systems to be completed no later than 08/01/22. In its Q3 21 10Q, the Company guided for the SCE deal to be an important driver of FY 22 results. The Company guided for the SCE deal to contribute $80.0 million at midpoint to Q4 21 revenue. Based on our understanding of representations made to us by the Company, the remaining $812.0 million contract amount is expected to be recognized as revenue in FY 22.[4]

Background on penalties for late completion and capacity guarantees: In its Q3 21 10Q, the Company represented it provided certain capacity guarantees to SCE and guaranteed completion of the SCE project by 08/01/22. The Company disclosed it would be obligated to pay liquidation damages for failure to achieve guaranteed capacity levels and/or substantial project completion by 08/01/22. In our view, penalties for late completion and underachievement of capacity guarantees highlight timely project completion risk and potential margin pressure.

> We are obligated under the EPCM Agreement to achieve substantial completion of all three facilities, subject to extension for customary force majeure events and customer-caused delays, no later than August 1, 2022 (the "Guaranteed Completion Date"). If we fail to achieve substantial completion of any of the facilities by the Guaranteed Completion Date, as extended, we are obligated to pay liquidated damages. In addition, we provided availability and capacity guarantees under the EPCM Agreement, failure of which entitles the customer to liquidated damages. (Q3 21 10Q)

We have the following concerns about the SCE project:

1. **Short project time frame highlights elevated timely completion risk, in our view:** In its Q3 21 10Q, the Company represented project construction periods were typically 12 to 36 months. Based on our understanding of representations made to us by the Company, work on the SCE deal began around the time the project was announced on 10/21/21. Given the Company guaranteed the project completion by 08/01/22, we believe the Company is targeting an SCE project construction period of approximately 9 months. **In our view, a historically short construction period highlights elevated timely project completion risk. Our concerns are heightened given the SCE deal is the Company's largest deal ever.**

[4] Throughout the course of our research, we communicated with Ameresco's investor relations department. We appreciate their timely and thorough response to our inquiries.

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> The contracts reflected in our fully-contracted backlog typically have a construction period of 12 to 36 months and we typically expect to recognize revenue for such contracts over the same period. (Q3 21 10Q)

2. **Supply chain constraints may drive project delays, in our view:** On its Q3 21 Conference Call, the Company represented several projects and its solar business were impacted by interruptions and delays due to industry wide-supply chain issues. The Company guided for supply challenges to persist in FY 22. We believe supply chain constraints may cause certain project delays and our concerns about SCE timely project completion are heightened.

> During the third quarter, several projects and our off-grid integrated solar business were impacted by interruptions and delays due to the industry-wide supply chain issues and COVID-19-related disruptions. It's important to point out that these issues primarily impact the timing of execution and that the delayed revenue will be recognized in later quarters. (CEO Mr. George Sakellaris, Q3 21 Conference Call, 11/01/21)

3. **Challenging labor environment may exacerbate timely completion risk & pressure margins , in our view:** In its article, "Construction worker shortage has reached 'crisis' levels" on 11/04/21, Housing Wire represented there was a US construction labor shortage crisis and guided for the situation to become more challenged in CY 22.[5] On its Q3 21 Conference Call, the Company highlighted it was able to hire consultants and was "not afraid" to do so on the SCE project. In our view, it may be challenging for the Company to complete its largest project in a historically short timeframe amidst a US labor shortage. Further, to the extent the Company is compelled to hire consultants to satisfy its SCE project labor requirements, we would be concerned about elevated labor expense and margin pressure.

> Interestingly, what we also have the ability to do and what was evident from kind of implementing this one was that **we actually have quite a few people we can tap to pull in on a consulting basis** as well. We're not afraid to do that. That cost actually doesn't hit our OpEx because they're 100% utilized. There's no real kind of overhead to think about with respect to those people. And actually going through the process that we've gone through in staffing this particular one makes me even more confident in our capability to take on more because we're recognizing that there are people there who really want to work with us. (CFO Mr. Spencer Hole, Q3 21 Conference Call, 11/01/21) [emphasis added]

4. **Assigning more senior employees to SCE project highlights elevated disruption risk, in our view:** On its Q3 21 Conference Call, the Company represented it shifted resources and more senior personnel to the SCE project to accommodate the accelerated timeline. In our view, reassigning additional senior personnel to the SCE project due to an accelerated project completion timeline highlights our concerns about the SCE project's historically short completion timeframe and timely completion risk. Further, we are concerned senior personnel reassignment may increase disruption risk on other projects and/or pressure SCE project margins.

> In order to execute this expeditious time schedule of this battery storage contract, we're shifting some resources, senior managers that they build in other projects to this particular project. (CEO Mr. George Sakellaris, Q3 21 Conference Call, 11/01/21)

5. **Low margin SCE deal may drive margin pressure, in our view:** In Q3 21, gross margin increased 330 basis points year-over-year to 21.5%. As of the date of this publication, the consensus expects Q4 21 (FY 22) gross margin to decline 50 basis points (280 basis points) year-over-year to 18.0% (16.5%). On its Q3 21 Conference Call, the Company represented design-build contracts, such as the SCE contract, typically generated a high-single digit gross margin. In our view, the lower margin SCE project may drive Q4 21/FY 22 margin pressure.

> As we have stated, design-build contracts typically yield gross margins in the high single-digit range. (CFO Mr. Spencer Hole, Q3 21 Conference Call, 11/01/21)

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5 https://www.housingwire.com/articles/construction-worker-shortage-has-reached-crisis-levels/

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Gross Margin Analysis	FY 22E	Q4 21E	Q3 21	Q2 21	Q1 21
Gross margin	16.5%	18.0%	21.5%	19.5%	18.6%
Year-over-year change	*(280 bps)*	*(50 bps)*	*330 bps*	*180 bps*	*50 bps*

6. **SCE project may create challenging FY 23 comparable periods:** As of the date of this publication, the consensus expects FY 22 revenue to surge 56.6% to $1,897.4 million and subsequently decline 18.1% in FY 23. While the Company indicated it had "quite a few" deals similar to the SCE project in its sales pipeline, the Company acknowledged those deals were smaller than the SCE project. In our view, FY 22 growth expectations are materially driven by the SCE project and rapid FY 22 growth may be unsustainable.

Revenue Analysis	FY 23E	FY 22E	FY 21E	FY 20	FY 19	FY 18
Revenue	$1,554.3	$1,897.4	$1,211.6	$1,032.3	$866.9	$787.1
Year-over-year change	*(18.1%)*	*56.6%*	*17.4%*	*19.1%*	*10.1%*	*9.8%*

Depressed Backlog Quality & Backlog Coverage May Portend Revenue Pressure

Background on backlog: In FY 20, fully contracted project backlog accounted for 26.8% of backlog, fully contracted O&M backlog accounted for 33.8%, and awarded, not yet signed project backlog accounted for 39.4%. Fully contracted project backlog represents signed customer contracts for project construction/installation. Fully contracted O&M backlog represents expected revenue under signed multi-year customer O&M contracts (all O&M backlog is fully contracted). Awarded, not yet signed project backlog represents expected revenue under awarded projects which have not yet been signed by the customer. In its FY 20 10K, the Company disclosed approximately 90.0% of awarded backlog historically resulted in a signed contract.

Backlog Analysis (as % of total backlog)	FY 20
Fully contracted project backlog	26.8%
Fully contracted O&M backlog	33.8%
Total fully contracted backlog	60.6%
Awarded, not yet signed project backlog	39.4%
Total	100.0%

Background on SCE deal: As mentioned, on 10/21/21, the Company announced it entered into an $892.0 million engineering, procurement, and construction contract with Southern California Edison (SCE) for the installation of three grid scale battery energy storage systems to be completed no later than 08/01/22. In its Q3 21 Earnings Release, the Company guided for the SCE project to be a meaningful driver of FY 22 results. Based on our understanding of representations made to us by the Company, the entire $892.0 million contract is expected to be recognized as revenue in Q4 21 and FY 22. Given the SCE deal was not included in Q3 21 backlog, we analyzed project backlog expected to be recognized in the next-twelve months relative to next-twelve-month project revenue expectations as of 10/20/21 (i.e. prior to the SCE deal announcement). While we acknowledge the SCE deal may drive FY 22 revenue growth, we are concerned the SCE deal may face unique challenges and drive margin pressure (discussed heretofore).

Total Q3 21 backlog levels increased slightly: In Q3 21, total backlog increased 3.4% year-over-year to $3,479.2 million. On its Q3 21 Conference Call, the Company highlighted a "significant pickup" in customer interest and bidding activity. The Company represented the SCE project was not included in Q3 21 backlog but guided for it to be included in Q4 21 backlog.

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Together with our $1.1 billion O&M backlog, we continue to have considerable long-term visibility to these higher margin revenue streams. Moving to our project backlog. We were very pleased to have increased our total project backlog 7% sequentially and 5% year-over-year to $2.36 billion as we continue to see a significant pickup in customer interest and bidding activity. Our recently announced battery storage contract with SCE was not included in the Q3 backlog number, but will hit our Q4 contracted project backlog. (CFO Mr. Spencer Hole, Q3 21 Conference Call, 11/01/21)

Backlog Analysis ($ in millions)	Q3 21	Q2 21	Q1 21	Q4 20	Q3 20
Total project backlog	$2,363.8	$2,210.9	$2,309.0	$2,214.3	$2,245.0
O&M backlog	$1,115.4	$1,121.2	$1,126.9	$1,131.1	$1,120.8
Total backlog	$3,479.2	$3,332.1	$3,435.9	$3,345.4	$3,365.8
Year-over-year change	*3.4%*	*(0.6%)*	*3.7%*	*(1.9%)*	*7.5%*

Fully contracted project backlog decline suggests backlog quality may have deteriorated, in our view: In Q3 21, fully contracted project backlog declined 24.7% year-over-year to $778.3 million. Fully contracted project backlog declined 1,310 basis points as a percent of total project backlog to 32.9%. In our view, a fully contracted backlog level decline suggests backlog quality may have declined. Our concerns are heightened given new bookings have historically been concentrated to Q2 and Q3 given the government fiscal year ends on 9/30.

Backlog Analysis ($ in millions)	Q3 21	Q2 21	Q1 21	Q4 20	Q3 20
Fully contracted project backlog	$778.3	$781.2	$787.8	$1,033.7	$1,017.7
Year-over-year change	*(24.7%)*	*(23.2%)*	*(25.0%)*	*(19.1%)*	*31.3%*
Fully contracted project backlog as % of total project backlog	32.9%	35.3%	34.1%	40.4%	46.0%
Year-over-year change	*(1,310 bps)*	*(1,050 bps)*	*(1,400 bps)*	*(840 bps)*	*1,060 bps*

Next twelve-month revenue backlog coverage decline highlights dependence on new contract bookings: In Q3 21, project backlog expected to be recognized in the next twelve months as a percent of next-twelve-month project revenue expectations as of 10/20/21 (i.e. prior to the SCE deal) declined 1,230 basis points year-over-year to 62.0%, 730 basis points below the prior three year seasonal average. In our view, depressed next-twelve-month project backlog coverage suggests revenue expectations (ex. the SCE deal) may be dependent on new contract bookings. While we acknowledge the Company entered an agreement with SCE on 10/21/21, SCE backlog was not included in disclosed backlog as of Q3 21, and the Company guided for the SCE deal to be an important driver of FY 22 results, we are concerned the backlog excluding the SCE deal relative revenue expectations excluding the SCE deal decline highlights ex-SCE revenue growth expectations may be difficult to achieve.

Backlog Analysis ($ in millions)	Q3 21	Q2 21	Q1 21	Q4 20	Q3 20	Q3 19
Next-twelve-month (NTM) project backlog	$551.6	$606.5	$607.0	$593.9	$605.9	$437.7
NTM project revenue (consensus estimate prior to SCE deal)	$889.5	$836.8	$824.8	$816.8	$815.8	$764.3
Next-twelve-month project backlog coverage	62.0%	72.5%	73.6%	72.7%	74.3%	57.3%
Year-over-year change	*(1,230 bps)*	*(70 bps)*	*940 bps*	*(110 bps)*	*1,700 bps*	*(1,900 bps)*

Depressed O&M backlog coverage heightens our revenue pressure concerns: In Q3 21, O&M backlog expected to be recognized over the next-twelve-months as a percent of next-twelve-month O&M expected revenue declined 720 basis points year-over-year to 70.6%, <u>the lowest level since Q3 19</u>. Depressed O&M backlog coverage

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heightens our concerns about the Company's ability to meet expectations.

O&M Backlog Analysis ($ in millions)	Q3 21	Q2 21	Q1 21	Q4 20	Q3 20
Next-twelve-month O&M backlog	$66.3	$67.0	$64.4	$64.0	$60.0
Next-twelve-month O&M revenue	$93.9	$89.0	$84.6	$79.9	$77.2
Next-twelve-month O&M backlog coverage	70.6%	75.3%	76.1%	80.0%	77.8%
Year-over-year change	*(720 bps)*	*(730 bps)*	*(700 bps)*	*(330 bps)*	*(740 bps)*

Elevated Contract Asset Levels Highlight Potentially Aggressive Revenue Recognition

Background on receivables, receivables retainage, and contract assets: The Company discloses receivables, receivables retainage, and contract assets (i.e. costs and estimated earnings in excess of billings) in its 10Q and 10K filings. In its FY 20 10K, the Company disclosed receivables retainage represented contractually withheld amounts due from customers until certain milestones were met. Contract assets represent revenue recognition in excess of billings under percent complete revenue contracts. Accordingly, we analyzed total receivables as trade receivables plus receivables retainage and contract assets.

Critical audit matter related to over-time revenue recognition highlights accounting irregularity risk: In its Report of Independent Registered Public Accounting Firm in the FY 20 10K, RSM US LLP identified percent complete project revenue as a critical audit matter due to the management judgement required to estimate project costs and profits. In our view, a critical audit matter related to percent complete project revenue recognition highlights contract asset and revenue recognition accounting irregularity risk.

> We identified the Company's accounting for revenue recognition under the project line of business to be a critical audit matter due to the significant judgments used by management related to the estimation of final construction profits. Estimating the final construction profit on these long-term contracts requires management to develop estimates of the total expected contract costs, including costs associated with labor, materials, equipment, subcontracting and outside engineering cost. Auditing management's estimates and assumptions involved a high degree of auditor judgment and increased audit effort. (Report of Independent Registered Public Accounting Firm, FY 20 10K)

Elevated total receivable levels may portend revenue pressure, in our view: In Q3 21, total receivables (including receivable retainage and contract assets)-to-revenue increased 15.8% year-over-year to 1.336, the highest seasonal level since the Company adopted ASC 606. The Company did not discuss receivable or contract asset levels on its Q3 21 Conference Call or in its Q3 21 10Q. In our view, elevated total receivable levels highlight potentially aggressive revenue recognition (discussed next) and may portend revenue pressure.

Total Receivables Analysis ($ in millions)	Q3 21	Q2 21	Q1 21	Q4 20	Q3 20	Q3 19
Total receivables	$365.8	$347.0	$324.6	$341.2	$325.9	$233.1
Revenue	$273.7	$273.9	$252.2	$314.3	$282.5	$212.0
Total receivables-to-revenue	1.336	1.267	1.287	1.085	1.154	1.099
Year-over-year change	*15.8%*	*(6.0%)*	*(15.0%)*	*5.6%*	*5.0%*	*31.8%*

Contract assets levels at multi-year seasonal high highlight aggressive revenue recognition, in our view: In Q3 21, contract assets as a percent of total receivables increased 320 basis points year-over-year to 58.4%, the highest seasonal level since the Company adopted ASC 606. In our view, the contract asset level increase to a multi-year seasonal high highlights potentially aggressive revenue recognition.

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Contract Assets Analysis ($ in millions)	Q3 21	Q2 21	Q1 21	Q4 20	Q3 20	Q3 19
Contract assets	$213.5	$195.0	$179.5	$186.0	$179.9	$124.7
Total receivables	$365.8	$347.0	$324.6	$341.2	$325.9	$212.0
Contract assets as % of total receivables	58.4%	56.2%	55.3%	54.5%	55.2%	53.5%
Year-over-year change	*320 bps*	*(880 bps)*	*(370 bps)*	*(970 bps)*	*170 bps*	*1,470 bps*

Contract asset level surge highlights potentially aggressive revenue recognition, in our view: The Company discloses revenue recognized from contract asset additions (i.e. gross contract asset additions) in its 10Q and 10K filings. In Q3 21, contract assets-to-gross contract asset additions surged 28.7% year-over-year to 1.569, the highest level since the Company adopted ASC 606. Given the contract asset-to-gross contract addition level surged to a multi-year high, we believe billing may have been delayed and/or certain contract asset related revenue recognition may have been accelerated and our concerns about potentially aggressive revenue recognition are heightened.

Contract Assets Analysis ($ in millions)	Q3 21	Q2 21	Q1 21	Q4 20	Q3 20	Q3 19
Contract assets	$213.5	$195.0	$179.5	$186.0	$179.9	$124.7
Gross contract asset additions	$136.1	$147.7	$130.3	$184.1	$147.6	$97.0
Contract assets-to-gross contract asset additions	1.569	1.321	1.377	1.010	1.219	1.285
Year-over-year change	*28.7%*	*1.0%*	*0.0%*	*(10.3%)*	*(5.1%)*	*109.6%*

Elevated receivable retainage levels may portend revenue pressure, in our view: In its FY 20 10K, the Company disclosed approximately 5.0% to 10.0% of invoiced amounts were generally retained until certain construction milestones were met. In Q3 21, receivable retainage as a percent of total receivables increased 330 basis points year-over-year to 10.8%, the second consecutive quarter receivable retainage accounted for greater than 10.0% of total receivables. In our view, elevated receivable retainage levels highlight elevated revenue recognized in advance of certain milestone achievement and potentially aggressive revenue recognition. Our concerns are heightened given retainage levels were above the Company's disclosed range.

Receivable Retainage Analysis ($ in millions)	Q3 21	Q2 21	Q1 21	Q4 20	Q3 20
Receivable retainage	$39.4	$36.5	$32.1	$30.2	$24.4
Total receivables	$365.8	$347.0	$324.6	$341.2	$325.9
Receivable retainage as % of total receivables	10.8%	10.5%	9.9%	8.8%	7.5%
Year-over-year change	*330 bps*	*420 bps*	*330 bps*	*350 bps*	*30 bps*

Depressed Contract Liability Levels May Portend Revenue Pressure, In Our View

Background on contract liabilities: In its FY 20 10K, the Company disclosed contract liabilities (i.e. deferred revenue) related to consideration received or unconditionally due consideration from a customer prior to transferring goods or services to a customer under the terms of a contract. The Company disclosed it generally recognized contract liabilities when advance payments were received and billings were in excess costs incurred on project contracts. Accordingly, we analyzed contract liabilities relative to project revenue.

> When we receive consideration, or such consideration is unconditionally due, from a customer prior to transferring goods or services to the customer under the terms of a sales contract, we record deferred revenue, which represents a contract liability. Deferred revenue, presented

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as billings in excess of cost and estimated earnings, typically results from billings in excess of costs incurred and advance payments received on project contracts. (FY 20 10K)

Depressed current contract liability levels may portend revenue pressure, in our view: In Q3 21, current contract liabilities-to-project revenue declined 11.9% year-over-year to 0.144. The Company did not discuss contract liability levels on its Q3 21 Conference Call or in its Q3 21 10Q. In our view, depressed contract liability levels may highlight aggressive revenue recognition and/or lower upfront payments and portend revenue pressure.

Contract Liability Analysis ($ in millions)	Q3 21	Q2 21	Q1 21	Q4 20	Q3 20	Q3 19
Current contract liabilities	$28.0	$26.6	$30.2	$34.0	$35.3	$23.2
Project revenue	$194.0	$196.3	$180.7	$244.8	$215.4	$145.9
Current contract liabilities-to-revenue	0.144	0.135	0.167	0.139	0.164	0.159
Year-over-year change	*(11.9%)*	*(38.0%)*	*(4.7%)*	*27.5%*	*3.0%*	*(31.3%)*

Contract liability reclassification highlights accounting complexity and irregularity risk, in our view: In its FY 20 10K, the Company disclosed it reclassified certain contract liabilities to contract assets due to customer payment timing.[6] In our view, reclassifications of contract liabilities to contract assets highlights revenue recognition accounting complexity and may increase accounting irregularity risk.

Changes in contract liabilities are also driven by reclassifications to or from contract assets as a result of timing of customer payments. (FY 20 10K)

Depressed Cash Flow Levels Highlight Elevated Earnings Sustainability Risk, In Our View

Depressed cash from operations and net income divergence highlights earnings sustainability risk: In Q3 21, twelve-month cash from operations increased $24.2 million year-over-year to negative $135.1 million, while non-GAAP net income increased 32.7% to $75.4 million. Cash from operations remained $22.7 million below the prior five-year average. Total receivables (including receivables retainage and contract assets) consumed $17.7 million of cash. In our view, non-GAAP net income growth despite persistently depressed and negative cash from operations highlights earnings sustainability risk.

Cash Flow Analysis ($ in millions)	12M Ended Q3 21	12M Ended Q2 21	12M Ended Q1 21	12M Ended Q4 20	12M Ended Q3 20
Cash from operations	($135.1)	($125.5)	($89.7)	($102.6)	($159.4)
Non-GAAP net income	$75.4	$72.0	$63.0	$57.9	$56.8
Year-over-year change	*32.7%*	*53.7%*	*35.6%*	*45.4%*	*96.8%*
Cash provided (consumed) by total receivables	($17.7)	($34.0)	$8.8	($17.8)	($91.7)

Historically depressed and persistently negative free cash flow levels heighten our concerns: In Q3 21, twelve-month free cash flow increased $8.6 million year-over-year to negative $340.5 million, the second highest free cash outflow in at least five years. Historically depressed and persistently negative free cash flow levels heighten our earnings sustainability concerns.

[6] We believe contract liability to contract asset reclassifications may relate to individual contracts moving from a contract liability position to a contract asset position due to contract estimate revisions.

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Free Cash Flow Analysis ($ in millions)	12M Ended Q3 21	12M Ended Q2 21	12M Ended Q1 21	12M Ended Q4 20	12M Ended Q3 20
Cash from operations	($135.1)	($125.5)	($89.7)	($102.6)	($159.4)
Capital expenditures	$205.4	$209.9	$210.0	$182.8	$189.8
Free cash flow	($340.5)	($335.4)	($299.7)	($285.3)	($349.1)

Elevated Insider Selling Heightens Our Earnings Sustainability Concerns

Elevated insider selling heightens our earnings sustainability concerns: In the twelve-months ended November 2021, CEO Mr. George Sakellaris (all directors and officers as a group) share sales increased 10.0% (17.2%) year-over-year to 1,270,887 (2,701,081), from an elevated base period. Elevated insider selling heightens our earnings sustainability concerns. Further, we believe elevated insider selling suggests the likelihood Ameresco is acquired in the near-term may be limited (i.e. we would not expect material insider sales immediately prior to an acquisition announcement).

Insider Sales Analysis	12M Ended November 2021	12M Ended November 2020	12M Ended November 2019	12M Ended November 2018	12M Ended November 2017
CEO Mr. George Sakellaris	1,270,887	1,155,142	400,000	--	--
Year-over-year change	*10.0%*	*188.8%*	--	--	--
All directors and officers as a group	2,701,081	2,303,790	841,480	530,987	223,099
Year-over-year change	*17.2%*	*173.8%*	*58.5%*	*138.0%*	--

Insider selling post-announcement heightens our concerns about the SCE project: From 10/22/21 (the day after the SCE deal was announced) to 11/22/21, insiders sold 239,479 shares. Insider selling post SCE deal announcement heightens our concerns about SCE project timeline achievability, unique challenges, and potential margin pressure. Our concerns are heightened given CEO Mr. George Sakellaris ceased selling shares from 09/09/21 to 10/21/21 (the day before the announcement) but began selling shares again following the SCE deal announcement.

Persistent insider beneficial ownership decline highlights reduced shareholder incentive alignment: As of 03/30/21, CEO Mr. George Sakellaris (all directors and officers as a group) beneficial ownership declined 570 basis points (1,080 basis points) year-over-year to 6.9% (9.9%), from a depressed base period. In our view, a persistent insider beneficial ownership level decline highlights reduced shareholder incentive alignment.

Beneficial Ownership Analysis	03/30/21	04/01/20	04/01/19	04/02/18	04/06/17
CEO Mr. George Sakellaris	6.9%	12.6%	17.0%	17.6%	17.6%
Year-over-year change	*(570 bps)*	*(440 bps)*	*(60 bps)*	*0 bps*	*90 bps*
All directors and officers as a group	9.9%	20.7%	26.5%	--	29.7%
Year-over-year change	*(1,080 bps)*	*(580 bps)*	--	--	*130 bps*

COVID-19 Driven Sales Cycle Extension, Inflation, & Labor Crisis May Pressure Margin

Extended sales cycle may delay revenue and drive certain margin pressure, in our view: In its FY 20 10K, the Company disclosed the sales cycle historically took 18 to 54 months on average. However, the Company disclosed the COVID-19 pandemic caused delays in its sales conversion cycle as customers adjusted operations and conserved cash. In our view, COVID-19 driven sales cycle extension may delay certain revenue and pressure margins.

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> Historically, the sales, design and construction process for energy efficiency and renewable energy projects recently has been taking from 18 to 54 months on average, with sales to federal government and housing authority customers tending to require the longest sales processes. **We have been experiencing a lengthening of our sales cycle as a result of the impacts of the COVID-19 pandemic, as customers move to adjust operations and conserve cash.** (FY 20 10K) [emphasis added]

Supply chain friction, inflation, and an industry labor shortage highlights margin risk: As mentioned, we are concerned supply chain friction may pressure results. In its FY 20 10K, the Company disclosed it may not be able to pass certain cost inflation onto its customers. In our view, supply chain friction, inflation, and the potential inability to pass cost inflation onto customers may drive margin pressure. Our margin pressure concerns are heightened given recently elevated inflation may not have been contemplated in certain, older fixed price contracts.

Vaccine mandate implementation may drive employee turnover and exacerbate labor shortage: In its Q3 21 10Q, the Company disclosed it was in the process of implementing a vaccine mandate for employees and subcontractors working on US Federal projects. While we acknowledge a federal judge blocked the vaccine mandate on 11/30/21, we are concerned the Company began implementing a vaccine mandate on certain federal projects and may have laid off unvaccinated workers. In our view, a vaccine mandate may exacerbate US labor shortage challenges and may drive (1) revenue pressure to the extent projects are delayed and/or (2) margin pressure to the extent the Company is compelled to hire higher priced contractors and/or increase wages to attract new employees.

> On September 9, 2021, President Biden issued an Executive Order requiring COVID-19 vaccinations for Federal employees. As a result, **we are in the process of implementing this mandate** for our employees and subcontractors who work in our Federal business segment. The vaccine mandate could result in a potential loss of employees or subcontractors who have not been vaccinated. (Q3 21 10Q) [emphasis added]

Other Observations: Non-Big Four Auditor, SEC Investigation, & Contract Expiration

Non-Big Four auditor highlights potentially elevated accounting irregularity risk, in our view: In its FY 20 10K, Ameresco disclosed its independent auditor was RSM US LLP. In its Report of Independent Registered Public Accounting Firm in the FY 20 10K, RSM disclosed it served as Ameresco's auditor since FY 10. The RSM audit partner working on Ameresco has no other public audit clients listed on the PCAOB website.[7] In our view and experience, engaging a non-Big Four auditor may increase accounting irregularity risk.

Ongoing SEC investigation: In its FY 20 10K, the Company disclosed it was the subject of an ongoing SEC investigation related to revenue recognition accounting for the Company's software-as-a-service (SaaS) business from 01/01/14 to 09/30/20. The Company does not disclose SaaS revenue separately in its 10Q or 10K filings. Based on our understanding of representations made to us by the Company, SaaS revenue is immaterial. While we acknowledge SaaS revenue may be immaterial, we are concerned the SEC investigation highlights elevated accounting irregularity risk.

> We are cooperating with requests by the staff of the United States Securities and Exchange Commission, or SEC, requested information with respect to revenue recognition for our software-as-a-service, or SaaS, businesses during the period beginning January 1, 2014 through September 30, 2020. (FY 20 10K)

US Dept. of Energy IDIQ expiration in April 2022: In its FY 20 10K, the Company disclosed it was party to an indefinite life indefinite quantity agreement with the U.S. Department of Energy set to expire in April 2022. While we acknowledge the agreement may be extended to December 2023 and renewal risk may be limited, we are concerned the April 2022 expiration highlights potentially elevated revenue disruption risk.

[7] https://pcaobus.org/resources/auditorsearch/engagement-partners/?engagementpartnermasterid=0004983545

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> Ameresco and our subsidiaries and affiliates are currently party to an IDIQ agreement with the U.S. Department of Energy expiring April 2022, which may be extended through December 2023. (FY 20 10K)

Historical debt covenant violation highlights historical default risk, in our view: In its FY 20 10K, the Company disclosed it was in default of one of its term loans for failure to maintain a debt service coverage ratio of at least 1.20. We are concerned a historical debt covenant violation highlights historical default risk.

> As of December 31, 2020, we were in default on one of our term loans for failure to maintain a projected consolidated debt service coverage ratio equal to or exceeding 1.20 to 1.00, however, a limited waiver was received in January 2021. (FY 20 10K)

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Risk to Our Thesis and Conclusion

Risks to our thesis: The following developments could present challenges to our thesis:

- The Company is acquired.
- Green energy/renewables shift drives long-term demand.
- FY 22 revenue/guidance materially outperforms consensus driven by the SCE project.
- The labor shortage, supply chain friction, and wage and cost inflation normalize with limited revenue/margin impact.

Conclusion: We are concerned there may be elevated risk associated with the Southern California Edison (SCE) project given the project is the largest the Company has ever attempted and is required to be completed in a historically short timeframe. Our concerns are heightened given the Company indicated the SCE project was lower margin. Supply chain friction and a labor shortage heighten our concerns about SCE project timeline achievability. In our view, a fully contracted backlog (excluding SCE project backlog) decline highlights backlog quality deterioration and depressed backlog coverage (excluding the SCE project) highlights new order book and burn dependency. We are concerned elevated contract asset levels highlight potentially aggressive revenue recognition. In our view, depressed contract liability levels highlight lower upfront payment requirements, potentially aggressive revenue recognition, and/or may portend revenue pressure. Depressed cash flow levels and elevated insider selling heighten our earnings sustainability concerns. We are concerned the COVID-19 driven sales cycle extension and inflation may drive project delays and margin pressure. In our view, a non-Big Four auditor and an ongoing SEC investigation may highlight elevated accounting irregularity risk.

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