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Transcript of
Pure Cycle Corporation
Second Quarter 2018 Earnings Call
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Participants

Mark Harding - President, Chief Financial Officer, and Director

Analysts

Bill Smith - Wm Smith & Co.
Bill Miller - Private Investor
Bill Cunningham - Private Investor

Presentation

Operator
Greetings, and welcome to Pure Cycle Corp's Second Quarter 2018 Earnings Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. [Operator Instructions]. As a reminder, this conference is being recorded.

I would now like to turn the conference over to your host, Mark Harding. Thank you. You may begin.

Mark Harding – President, CFO and Director
Thanks very much. Good morning, or good afternoon, depending on what part of the country you're in. I would like to welcome you all to our mid-year earnings call. We have got a slide deck for this call which you can all find on our website. So if you go to purecyclewater.com and you go over to the Investor page, then there will be an icon that will allow you to click open the presentation and follow along with us on the presentation. I will try and note the transition of the slides as we walk through the presentation.

So with that, I would like to get started. We will have some prepared remarks and then we will open it up to some Q&A towards the end of the call. The first slide is always to get the lawyers out of the room, so it's our Safe Harbor statement that says that statements that are not historical facts contained in this corporation are forward-looking statements in the context of the meaning of the Private Security Reform Act of 1995. You all, I am sure, are very familiar with that.

So we will move on to kind of an overview of the company, and I'm going to blow by this pretty quickly because most of you will be familiar with the company and what operations that we play with. But we are a water utility company. We have a portfolio of water that we own or control, so water outlets is one where you can own that asset as a real property asset. We generate revenues on that from selling water to customers, both residential customers, commercial customers, as well as industrial customers. A large segment of that is to the oil and gas industry, and then we also own some oil and gas royalties where we receive some mineral royalties from oil and gas interests in these properties that we have.

Moving on to the fourth slide. We are sort of cradle-to-grave on the water utility. We own the water, the wells that divert that, they are treated, distributed to our customers. They use it, they turn it into a liability, and we collect that. We reprocess that water and then we reuse that water for irrigation and industrial uses.

Our portfolio can serve about 60,000 connections, and the metrics on that, we generate revenue from that, tap fees, which are a one-time capital fee, and then we also generate revenue from monthly water and sewer bills. So we typically get about $30,000 per connection on the water and the wastewater side on the tap fees and about $1,500 per connection annually in water and wastewater revenues.

Transitioning to the next slide, really what we want to talk about more specifically is the development side. We have about thousand acres, 930 acres of land, located in a very good location in the Denver Metropolitan area, right along the interstate. We are about four miles south of Denver International and about 16 miles just due east of Downtown Denver, a nice piece of property. We have got a diamond interchange at the property, which give us good transportation access. The property is zoned for about 4,400 residential homes, and that's a mix of detached single-family homes, attached paired product and multi-family homes, as well as about 1.3 million square feet of commercial area.

Moving on to the next slide. It gives you an overview of where we position ourselves in the Metropolitan area, a very good job project for us. We have got a lot of employment centers in and around our area. So, our target for this is going to be kind of entry-level housing and some of the logistics that are important to those buyers are going to be access to transportation and access to employment centers. So you have the Denver Airport, which is the largest employer in the state, that's about 35,000 jobs, we have an Amazon Distribution Center, it's about 1,000 jobs. We have some convention center hotels that are opening up in the fall that are very big employers as well, as many as 3,000 jobs. So really, most of the concentration of activity in the Denver area is concentrated in this I-70 corridor, so we're very excited about bringing this project online.

Transitioning you to the next slide, really I want to detail out a little bit about what's going on. We did open construction on that. We're very excited about being underway, doing our over excavation and our overlot grading of these lots. The over excavation and grading component of this will probably last about three months, so we are actually grading the entire 150 acres as the mass balance works on how you deliver these lots and the efficiency of delivering these lots, because you cut and fill and moving the dirt so that it's very difficult to move that for one specific neighborhood. The plan on that is to do the over-ex and the grading for, well not the over-ex, some of that over over-ex will be in phases, but the overlot grading will be for the entire 155 acres, or the entire 500 lots.

We're concentrating the over excavation, which is really a soil mitigation issue, so Colorado has some expansive soil. This particular site is really what we would call marginal on its expansive soils, but most of the builders are responsible for their own evaluation, an independent evaluation of whether or not each of their individual lots requires this type of soil mitigation procedure, and they handle that cost themselves. They use the same contractor that we use for our overlot grading under a separate agreement with them, but we're concentrating our activity to this brown area, which really will deliver about 220 lots.

So we're looking at not only the dirt work on that, on the over-ex, but we'll have the utilities, wet utilities, which will be water, sewer, storm, dry utilities, which will be communication and electric, all configured for that first 220 lots. If we have that over-ex probably by sort of mid-to-late June, we will be done by that timeframe. We will be letting contracts, probably later this week for some of the wet utilities to get the water, sewer and storm drain facilities and some of the channel way work done, a lot of the electrical probably following shortly thereafter, really to just build to getting some sites that are available.

So working with our three builders, we want to try and deliver some model home lots. We have the ability for them to start construction on those sometime later this year and then really work on production of those starting for the next building season starting in January. But we will have sort of delivery of lots later this year, where they will be buying, some of them will be buying. Just in two of the three builder cases we have lot development agreements, which means we get progress payments. One payment when we deliver platted lots, one payment when we get the completion of the wet utilities and then a third payment upon completion of the finished lot, and then with one builder finished lot deliveries directly.

So, look to see some of activity in follow-on quarters later this year and then really rolling into first quarter of next year. The overlot grading is going very well. Sometimes when you get started on that in the winter, particularly for seasonal issues out here in Colorado, you can be influenced by bad weather, and while the East Coast, all of our friends and investors on the East Coast have had a horrific year in dealing with weather issues, ours has been very mild, so you guys have been getting all of our snowpack this year. Most of our contractors are probably even a little ahead of schedule on some of those deliveries, so we're excited about maintaining that delivery schedule.

Moving on to the next slide, talk a little bit about where do we go from here. We're really working on the first 500 lots, and I think we have got a very good execution on how we are delivering those first 500 lots. But we're also looking at, this is a bigger project, we have got about another 800 acres to deliver on this and how do we phase some of that activity. This will give you a little bit of work that we have been doing on that phase, so we're looking at the second phase, which will be starting with some of the commercial, up by the interstate and then flowing down into more residential and cluster type development for a number of different builders.

We have three builders in our first phase and we're looking at adding additional builders in there to, maybe as many as six different homebuilders, as well as some commercial type builders where they are building commercial and retail installations up along the interstate. So we're working our way through our land plan on this one and hope to show that to some of our builders later this spring, early summer to start getting engaging level of interest and finalize that plan and working that through the process through this year and then being in a position to where we can take a look at multiple phases going on at the same time, as we're starting to deliver lots for our first phase, we can start working on some of the grading activities for our second phase. So that will give you the high level of some of the development activity and really some of the areas of focus of what it is that we are doing on that.

Let me move on a little bit and talk a little bit about another major activity for us, which is really providing water to the oil and gas industry for well stimulation and some of the activities that we are seeing this year. We have got multiple operators in the field now. There has just been a little bit more competition for drilling out these leases. So we have got, I think as many as three, maybe even four different operators in this area that are looking at some of the well activities.

Our more well-established operator is more active than the others, and they are projecting out the highest number of wells, maybe as many as 20 wells, and then we'd probably get three to eight wells from some other operators in the field, so we'll see how that activity looks. We're protecting somewhere around 23 wells as a conservative estimate for the fiscal year.

Average sales on these wells, so some of the newer entrants in here are actually using some alternate design, frac design concepts, which use a little bit more water. So on average I think we're seeing about $150,000 per well. We historically have seen about $100,000 a well. This added that technology and how they plan and stage these fracs are evolving, and I think that has something to do with both the technology as well as this field in specific.

So very excited about that. We had some good operating results for the first six months. We will highlight a little bit later, but it still seems to be a very active field for development. Most of this activity continues to be HBP, hold by production type drilling. We haven't seen a whole lot of field development, and really the difference between HBP and field development will be the number of wells per pad, where you can see as many as a dozen wells per pad, which makes it very efficient for them on drilling and fracking activity and then correspondingly a heavy water use for us on the transfer of water to those operations.

The next slide really talks a little bit about the field, multiple formations, multiple drilling activities and then kind of the revenue that we see on the water activity per well.

Moving on to the next slide. This is really just kind of follow-up report card on our Wild Pointe acquisition, so that continues to go very well. We had, I lost my number on this, the number of tap fees on that, so forgive me while I catch up to my presentation. We have got continuing builder activity from the project, so we have get two types of development out there, residential development, which I think there is still probably about another 60 to 70 lots available from the residential activity. That's seasonally derived, where you have a little bit of activity.

We have only had a couple of tap sell deliveries, as you see. Those taps are about $15,000 a tap, and that's because the water system is already fully developed, so typically we see about a 50% margin in that from the water supply to the water infrastructure, so all that water infrastructure was already capitalized by the previous developer we acquired this from. Usage fees out there are fairly seasonal, so what we see is the tail end of last year's irrigation season and then really a limited amount of in-house demand over the winter.

Those typically spike over the summer just because of those seasonal deliveries, but still very, very happy with the acquisition. It continues to perform in line with our forecast of the model assumptions on the acquisition itself. And we still do have our nets out for other opportunities. I know that question comes as to where are the opportunities, and we try and focus those in areas where our current assets are. So we are still talking with a number of opportunities in that area to add those acquisitions.

Next slide is going to talk a little bit about our WISE system. We continue to highlight this because it's part of our major infrastructure and delivery here, so in addition to pipeline capacity where we have about three mgd of capacity on our transmission line that goes really along the southern portion of the Denver Metropolitan area, we also get some water out of that. So that allows us to expand our water service obligations both for our residential as well as our industrial customers.

And then, as we look at the regional opportunities here, really the advantage of this system and this cooperative is that we’re interconnected with 13 different area water providers and it enhances opportunities amongst all of us for our infrastructure, our supply capacity, our storage capacity. So we look to expand upon this system and these opportunities over time as well as we look at how systems grow and how our opportunities mature over time.

We will go to slide 13, which will be the bullet on the quarter. We summarize it out, our income almost up two-fold over prior-year income, so about $2 million. A good portion of that, $1.6 million is going to come from frac revenue, so that shows you where that activity is. I think we will see continued strength here, maybe even a little bit of growth in this opportunity just because they don't have quite as much activity over the winter months as they do over the summer months.

So we’ll see if we have sustained opportunities here, it will still round out for a very good year end for us. Our municipal water, wastewater service is in line with last month. Some seasonality in here, but really there is no variable differences in the increase here. Tap fee revenues, again, some of those taps are attributable to Wild Pointe and some of those taps are attributable to an existing customer, which came into the system as well, added existing capacity in the system.

And then some of our oil and gas royalty revenues, those are down a little bit and then it continues to be operational issues with the wells themselves. As these wells continue to mature, the operators continue to refine how they are operating. And we still are under a gas driven well, so I think we’re one of the last wells still yet not to have a pump jack on the system. So it still produces good royalty revenue, about $25,000 a month, as they get a full month worth of operation.

The last two sheets are really our balance sheet and income statement. I won't go through those. You guys can look through those. We still have a very good liquidity position. We have about $24.5 million in liquidity in that, so we feel we have sufficient capital to fund the development of lots out at Sky Ranch, and we try and make sure that we have a good cushion in reserve in case there is any variances in timing of deliveries or otherwise. But we're very excited about being able to deploy those capital and be able to push out some of that for returns in our shareholders.

With that as a summary, let me turn it back over to our moderator, and see if we can have some questions that you all might have to drill down on some of the specifics of what it is that we're doing.

Operator
[Operator Instructions]. Our first question is from Bill Smith with Wm Smith & Co. Please proceed with your question.

Q: Hi, Mark. Congratulations on your progress. With the announcement of Aurora Highlands and Aerotropolis and the agreements with Adams and Arapahoe and Denver counties, what impact do you think that could have on Pure Cycle and on your water over the next several years? We are talking 60,000 residents, I think, is what they are talking about, a whole new city.

Mark Harding – President, CFO and Director
Yes. What that really illustrates, Bill, and thanks for the question, the Aerotropolis, if some of you have been following the local press on that, it's really a development that's, I would say, three miles west of our border. So it really is very close to where Sky Ranch is, and it has a couple of advantages. Certainly, if it's in the city of Aurora, they are going to get their utilities from the City of Aurora. But what really it shows you is the emphasis that the I-70 corridor is receiving from almost every segment, whether that's residential, whether that's commercial, whether that's employment, all of the energy is really being spent in this corridor, which that's the tide that lifts all boats.

So we're very excited about that. They are not in the ground, so they have got a few, I would say, maybe a couple of years before they start breaking ground on some of their major developments. That's not to say that they don't have some builders that are already working on projects that are either adjacent to or in proximity to that particular development, but what it really does is it brings more demand for activity in the corridor.

The second side of it is, it's going to expand the Aurora utility system. Then there is opportunities for us to participate in regional assets, whether that's extensions or expansions to the WISE agreement, or whether that's stories opportunities, or a number of other areas. So we'll wait to see what happens with additional opportunities as it relates to utilities, where Aurora, Denver and the South Metro Group can work together on efficiencies on delivering water utilities to the region as well.

So it's a very exciting project. It's very exciting for us because it's bringing more investment into the corridor. I think those price points will be a little bit higher than ours just because of the level of what that overall project is looking for. We don't look at it as a direct competitor to our lots out at Sky Ranch, but it does certainly add more emphasis to it.

Q: In terms of selling water, you have 27,000 or 28,000 acre feet of water that can serve 60,000 homes, at $30,000 a tap and $1,500 sewer fees, isn't that a new market for your water assets then? Wouldn't that be a new market?

Mark Harding – President, CFO and Director
Probably not, Bill, mostly because it's going to be in the City of Aurora. So those are utilities that are going to be provided by the City of Aurora, but there are a lot of adjacent properties to that. And the reason we are excited about the energy that that produces for the I-70 corridor is it puts more of those lands into play, and so those are opportunities for us to be able to extend service to the adjacent properties where they don't get their utilities from the City of Aurora. And they would logically be extending our system, and very cost-effective for us to extend our system to the adjacent properties than be able to incrementally provide water and sewer service to them, not necessarily Aerotropolis, but a lot of the adjacent properties.

Q: And would that maybe bring into play the reservoir that you have kind of gone back and forth on for a number of years with Aurora, could that bring that into play in terms of storage capacity that they might require?

Mark Harding – President, CFO and Director
It could. It grows that system. And so whether it's our storage, whether it's our supply capacity, whether it's our peaking capacity, there could be not just storage but many other opportunities as you look at regional cooperation.

Q: Okay. What do you think your revenues could be over the next, say, two years with the activities that you have found what you are looking going forward? Do you have any thoughts on what that might be?

Mark Harding – President, CFO and Director
The thump in the room was my controller falling off his chair going, no, no. Good question. It's difficult for us. What we look to, I will give you the areas of our revenue. Take a look at the oil and gas stuff, so I think our oil and gas revenues continue to strengthen. This year, the first six months we had $1.5 million. I think we get a little bit better for the next six months, so maybe we get between $3 million and $4 million in oil and gas revenue this year.

Where does that project for the next two years? We're still in HBP drilling. So if oil continues to remain strong, I think you start to convert over to some more field development. So that number could strengthen very nicely for us. I hate to give guidance on that, but you can do your own sensitivity analysis on that and say, okay, if we had two rigs doing HBP wells, that could be as many as 40 to 50 wells a year, so you can do the math on that and see how that sustains itself over a period of time. That's the oil and gas activity.

As we develop lots, we are going to be selling lots, we'll get some revenue for lots this year. I don't want to give too much guidance on that. We have contractual issues with the builders and they will be buying X number of lots, and I don't have those numbers off the top of my head. But let's say we sell—we'll have more revenue coming in, in the various stages, so I can say, on the lot development agreements we might sell 100 lots in the lot development side. We might sell 50 or 75 lots on wet utilities, and then might sell maybe 50 lots on finished lot deliveries in two of the delivery agreements, and then maybe 25 to 35 finished lot deliveries with another builder. So those are at that $70,000 to $75,000 number. And then as they apply for building permits, then we'll get those tap fees attributable to those and then the recurring revenue following up on those.

So it starts to ramp pretty quickly because when we're getting a couple hundred lot sales over a period of time between the real estate side and the tap fee side, that could be close to $100,000, and then you combine that into the oil and gas revenues, things start to look very exciting.

Q: Yes. And one other question. The six builders, you started with three. It sounds like you have a potential up to six now. Is there a reason that that's been extended? Is it to accelerate development? What was the reason for that?

Mark Harding – President, CFO and Director
Yes, for two reasons. One is that we will have a bigger footprint in the second phase of this, so instead of us having 500 units we might have as many as 2,500 units. And there will be a cross section of products, so we'll have standard detached product, which we have now, we'll have some sort of alley load product, which is going to be higher clustering of density. We will have paired product, which is going to be side-by-side units, there are some builders that have very nice product that they want to build in a paired product standpoint, and then we will have maybe multi-family builders.

So you have a number of different players that are in each of those segments in addition to the portfolio of standard detached single-family home builders. So it's not that we're ramping up, it's just that we have more product offerings to make available to the market.

Q: Great. Thank you, Mark. Congratulations on your progress.

Mark Harding – President, CFO and Director
You bet. Thanks.

Operator
[Operator Instructions]. Our next question is from Bill Miller, a private investor. Please proceed.

Q: Mark, hi. It seems to me, just looking at your --

Mark Harding – President, CFO and Director
Good morning or good afternoon.

Q: Good morning, good afternoon, good evening, whatever. Just looking at your balance sheet, your outline of what cash flows could be, you are going to have a great deal of cash. I guess I have two questions. One, what are you going to try to emphasize as we look out over three to five years, recurring revenue lot sales, which are one-time and with the recurring revenue, which we hope you are going to generate, why aren't you thinking about and maybe even at this time, going to buy back stock? Dividend, I don't care about. But buying back stock, I do care about. Is that something that is on the table, or is it off the table? Are you going to have to wait for a while? What are the elements that go into that decision, and when do you think it will take place?

Mark Harding – President, CFO and Director
Boy, that's a good, probing question, a tough one. So nobody can accuse you of giving me a softball here, Bill.

Q: Well, I wouldn't want to. You're used to softball questions.

Mark Harding – President, CFO and Director
Well, yes, sure. Let me talk ideologically, or philosophically. Certainly, the high quality problem is we are going to have a good balance sheet to consider options with. So we are thrilled about that, and we are thrilled about really demonstrating that return for our shareholders. And then it becomes how effective are we going to utilize that, are there other opportunities for us to invest into, that magic word of yours is recurring revenue, are there opportunities to invest in where a company can utilize its assets for more of those recurring revenues?

And those are the acquisition side of things, where we can find opportunities to connect existing systems, be able to leverage our supply capacity to bring new supplies to them and expand the number of connections that we get beyond just Sky Ranch. Sky Ranch is great, we are vertically integrated there, we can control the timing and develop and bring those customers online into the market, but we would like to have more Sky Ranch's going on concurrently. So, you know, there is opportunities, as Bill Smith brought up, with the neighboring property owners, where we might be able to expand our systems and have multiple projects going on at the same time and organically serving new connections.

But then how about existing connections? And so kind of like what we saw with Wild Pointe, are there opportunities for us to pick up existing systems and be able to serve water to them as well as manage and maintain their existing operations? So that's probably the first area of interest to management and to our Board, as we look at, if we can't find good opportunities there and we build the continuing balance sheet and find out opportunities where we can return those back to our investors.

The value of our stock is important. If the market isn't able to appreciate what all you folks understand and appreciate by seeing the capacity and the opportunity with holding this stock, then that's certainly an option. Buying back shares on an undervalued stock is certainly something. I can't speak for the Board. Those are Board level decisions, notwithstanding whatever it is that I think is a good idea, they are going to make that as a policy issue.

And then lastly is the dividend. We are a water utility company and people own water utility companies because they also provide dividends. And so we look at dividends from recurring revenue as opposed to the capital base, but there is opportunities for that.

So all those options are on the table and we like to be able to discuss those with the high quality problem of having the money to do something about it.

Q: Mark, do you think there are a lot of opportunities for recurring revenues in the Metropolitan Denver area where they have a good system, but guess what, housing is expanding faster than their water supply, and therefore, you can sell them new and higher quantities of water, or do you have to buy the whole system?

Mark Harding – President, CFO and Director
So buying the whole system or operating the system, there is a number of ways that you actually can do that that don't require them having to transfer deed ownership but you get the same effect. That's kind of how we structured the Wild Pointe acquisition. Yes, there are a lot of those opportunities in the Metropolitan area. We are careful about how we look at those, how we model those, what type of an investment we need to bring to the table in order to make those transactions work.

A lot of times it's much beyond just the existing system itself. They have other, sometimes these are deferred maintenance systems. And so when we look at them, we sort of say, we would need to make these investments and then it's a matter of walking them through the realities of what it is that they have and what we can bring as value to the equation. Certainly, our ability to operate systems is of value, but they are operating their systems to a certain degree. A lot of times they will rob Peter to pay Paul. And if there is something going on in public works that needs capital as opposed to the public water utility, sometimes those cross over and it's a piggy bank for them that may or may not be, it has a short-term opportunity but long-term deferred maintenance opportunities. So we evaluate those situations as well.

So it's a very dynamic process. You would think acquisitions are all about price, but they are not. Not in this industry. There is a lot more factors that go into evaluating those systems. So I am excited about those. Hopefully we will have some of those opportunities that we can announce this year, but we are fairly selective about how it is that we are going after those.

Q: Mark, why can't you increase the price of your water? It's becoming an increasingly scarce commodity, even without droughts which you are having, so why can't you increase the price?

Mark Harding – President, CFO and Director
Pricing is a sensitive topic for us and our customers. When you take a look at the price that a homeowner pays, you're in a fairly monopolistic environment. It's not a monopoly, but that customer has a hard time replacing your water supply, so we're cost sensitive about those rates per kgal on our users. We try and attribute that to the actual usage per individual house, not only in terms of the tap fee but also it's easy for us to be able to say, okay, this is the meter deliveries for that particular house.

If you take a look at some of those customers that don't pay tap fees that are sort of at the market on that, that's mostly going to be our oil and gas customers. And we are delivering continued value to them. So as we add more system capacity, we make more of our system available for their use, we add assets to that as it relates to pipelines and reservoirs, then all that stuff really does go into our calculus on the rate that we charge them. So I would say we do see rate increases and we see rate increases each year for those customers.

The perceptual value or scarcity value in a drought year versus a wet year, we try not to market our pricing based on that type of activity. But when you have sustained dry years, you have more assets that come into play, so then that naturally comes into the pricing equation of what it is that you are selling your water for. So we do have a very sensitive customer in that and then we also have a very sophisticated pricing methodology that really connects both the commodity, being the water supply, as well as the infrastructure that's delivering that so that somebody is paying the appropriate rate.

I will tell you unequivocally and this is categoric in our industry, is that people don't appreciate the value that they get in getting clean water to a single-family house. The amount of technology and investment and sophistication that goes into that, we should be paying three times what we are for the privilege of getting clean water. And there is not a water manager or CEO of a water company that wouldn't tell you the same thing, but by the same token, it's one of those commodities that people assume to have value for, so there is a delicate balance there.

Q: So what do you think you will be able to increase the price, with inflation or with some other --?

Mark Harding – President, CFO and Director
No. We do better than inflation just because of the assets that we continue to add into the equation. So I can't say that you can plan on a 6%, 7% increase in water rates over time. You may see that. You may see that in the tap fee. You may see that less, more of a cost of living index as it relates to the monthly fees, but as more development continues to constrain the market and continues to make water availability even more scarce, those tap fees are going to go up, Bill. And they are going to go up for everybody, they're not going to just go up for us. So on a comparative market, getting your tap connections from Pure Cycle as compared to getting your tap connections from any of the other hundred different water providers in the Denver area are all going to go up more.

Q: And what about the commercial properties, can you charge them more?

Mark Harding – President, CFO and Director
Well, we typically gauge that based on the amount of water used. And I am agnostic as to if that's a single-family house or a bottling plant or brew pub, they are going to pay the same rate based on the amount of water, so the customer is agnostic too. It's just a use calculation.

Q: Okay. Great. Thanks.

Operator
Ladies and gentlemen, we have reached the end of the question-and-answer session. I would like to turn the call back over to Mr. Harding for closing remarks.

Mark Harding – President, CFO and Director
Actually, let's see if we can take one more call or one more question.

Operator
We did just get one in there. This is Bill Cunningham, a private investor. Please proceed.

Q: Hi, Mark. How are you?

Mark Harding – President, CFO and Director
I am great. You made it just in the wire.

Q: Yes, well, I tried earlier. Apparently, it didn't take. So when they said, there were no more calls, I pushed for a second time and it worked that time. I am actually looking at trying to sort out from an analytical point of view, the potential profitability of Phase 1 and I am looking at slide 7, where you have your infrastructure costs, etc., on the right-hand side there. And I guess for starters, you ultimately collect a little over $100,000 per lot, with $70,000 or so for the payment from the builder and another $30,000 or so for the tap fees. Is that right?

Mark Harding – President, CFO and Director
Right. That's right.

Q: Okay. So we are talking gross $50 million there. Then I am looking at the cost items. The Monaghan Road, $2 million. That will actually, it's going to be of benefit to Sky Ranch for more than this particular section. Is that correct?

Mark Harding – President, CFO and Director
Yes. That's right. Some of these investments, most of the offsite investments, actually the four of the six that are really labeled here do benefit more than just our first 500 lots.

Q: Yes. That's exactly where I was going with my questioning. So probably fair to say no more than half of the Monaghan Road $2 million would be allocated to this section, maybe even less than that?

Mark Harding – President, CFO and Director
Well, that's certainly the full cost of it, and then the capacity can be probably about maybe another 30% at some point. So what we are doing on Monaghan, if we start to drill down in the weeds on this, we are building three of the six lanes on that and those three lanes will handle traffic up to about 800 units rather than 500 units, to give you just some capacity numbers.

Q: And then the drainage, it looks like that's entirely this section that's impacting that.

Mark Harding – President, CFO and Director
It is, but it receives drainage from the other sections. So as you see that line, that line continues on and it goes up front, so the size of the pond is actually for the full drainage allocation.

Q: Okay. So this will be a minimal expense probably in some of the other sections that you develop.

Mark Harding – President, CFO and Director
Exactly right. That's what it exactly translates to.

Q: Okay. And then the wastewater facility and the water storage treatment facilities, are they going to be for the entire Sky Ranch, or just for this section?

<u>Mark Harding – President, CFO and Director</u>
No. They are in their master planned locations, but they do have some micro phasing in them as well. So the wastewater plant can handle probably about 1,000 connections. Similarly, the water and wastewater are really designed for about 1,000 connections on this phase. And as you always know on construction projects, it's more expensive to come out of the ground, so it's not as though the next 1,000 connections cost us another $5 million. I think our buildout for the wastewater treatment plant is somewhere around $12 million. So the next increment is much, much smaller than the first increment.

Q: Okay. Good. And then obviously the overlot grading is pretty straightforward, that's $15,000 a lot.

<u>Mark Harding – President, CFO and Director</u>
Right.

Q: And then the roads, curbs, other utilities, actually it's all utilities, right, because it's your sewer and water connections that are in that number?

<u>Mark Harding – President, CFO and Director</u>
That is the retail system. Yes.

Q: Excuse me?

<u>Mark Harding – President, CFO and Director</u>
That's the retail system in all the streets of the subdivision itself.

Q: Yes. And what's your responsibility for the water and sewer lines? Is it to the homes, or is it to the property lines?

<u>Mark Harding – President, CFO and Director</u>
To the property line.

Q: Okay. Very good. That's great. Very helpful. Thanks.

<u>Mark Harding – President, CFO and Director</u>
You bet. Thanks.

<u>Mark Harding – President, CFO and Director</u>
So if any of you who wanted to ask a question didn't quite get in or the technology wasn't allowing you in, certainly feel free to give me a call. I have been dilatory on not being out on the road much over the last six months. So hopefully as things get more open, it will free up a little bit of time for me to get out to the various markets, New York, Boston, Chicago, out to the West Coast as well, just to kind of meet with folks and catch them up a little bit, not only of what we are doing and also maybe what it is that we are planning for our second phase.

One of the things that we are going to try to do is have a day here for those that have an interest that can come here. There is nothing like seeing this with your own eyes, seeing the grader, seeing the streets come in and seeing some lots being delivered. So that's something that we will put some thought into. We will send out maybe some invites to the market or a press release and then really kind of collect some interest on folks that might like to come out and do a day here, see what's going on, not only on the residential side but see a little bit more of our system, see a little bit more some of how we are delivering water to the oil and gas industry and those types of things. So be on the lookout for something towards the latter part of the spring for a date sometime this summer on that.

So with that, I want to continue to thank you all for your support and confidence in management as well as our Board, and if you have anything that comes up, don't hesitate to give me a holler.

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