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ROCK - Q4 2014 Gibraltar Industries Inc Earnings Call

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PRESENTATION

Operator

Good day ladies and gentlemen and welcome to the Gibraltar Industries fourth-quarter 2014 earnings conference call. Today's call is being recorded and webcast. My name is Kevin and I'll be your coordinator today. (Operator Instructions).

I would now like to turn the call over to your host for today Mr. David Calusdian from the Investor Relations firm Sharon Merrill. Please proceed.

David Calusdian - *Sharon Merrill Associates - IR Representative*

Good morning, everyone, and thank you for joining us. If you have not received a copy of the earnings press release that was issued this morning, you can find it in the investor info section of the Gibraltar website, Gibraltar1.com.

During the prepared remarks today, management will be referring to presentation slides that summarize the Company's fourth-quarter performance. These slides are also posted to the Company's website.

Please turn to Slide 2 in the presentation. The Company's earnings release and slide presentation contain forward-looking statements about future financial results. The Company's actual results may differ materially from the anticipated events, performance, or results expressed or implied by these forward-looking statements. Gibraltar advises you to read the risk factors detailed in its SEC filings which can also be accessed through the Company's website.

Additionally, Gibraltar's earnings release and remarks this morning contain non-GAAP financial measures. Reconciliations of GAAP to adjusted measures have been appended to the earnings release.

On our call this morning are Gibraltar's recently promoted Chief Executive Officer, Frank Heard, and Chief Financial Officer, Ken Smith.

At this point, please turn to Slide 3 in the presentation and I'll turn the call over to Frank.

Frank Heard - *Gibraltar Industries, Inc. - CEO, Director*

Thanks, David. Good morning, everyone, and thank you for joining us on our call today.

Gibraltar closed 2014 with a solid fourth quarter. Net sales exceeded the high end of our guidance, growing 7% year-over-year. Adjusted earnings per share came in near the top end of our range at $0.02 per share. The Company's revenue growth was driven by increased sales of our postal storage plus roofing related products in the residential products segment while the combined demand from industrial and transportation infrastructure markets remained weak.

For the full year, net sales were up 4%, at the high end of our previous guidance, and full-year profits matched the high end of our guidance at an adjusted $0.47 per share. With that said and speaking for our entire leadership team, our goals are to achieve stronger financial results, make more efficient use of capital and deliver higher shareholder returns. If we expect to make meaningful progress towards achieving these goals, we will need to be aggressive in three key areas.

The first is operational excellence. The second is portfolio management and the third is to make effective use of acquisitions as a strategic accelerator for the business. I'll discuss our strategic plan, which includes these three key areas, and provide some thoughts on 2015 after Ken reviews our financial results. Then we'll open the call to any questions that you may have.

So with that, I'll turn the call over to Ken.

Ken Smith - *Gibraltar Industries, Inc. - SVP, CFO*

Thanks, Frank, and good morning. Now let's turn to Slide 4 titled "Consolidated Results". As Frank pointed out, fourth-quarter revenues were up 7% year-over-year as the unit volume increased sales by 700 basis points while pricing contributed a positive 90 basis points while foreign currency effects reduced revenues 90 basis points.

The fourth quarter's adjusted operating income and EPS were lower than last year and did not benefit from this quarter's volume increase. The largest unfavorable factors were the shortfall in our planned capacity expansion for postal products followed by a continuing weak environment for broad-based price increases by which to offset inflationary costs that we absorbed. And lastly, a less profitable mix within our industrial and infrastructure segment.

Next but before describing the performance of each segment, I do want to comment on the fourth-quarter non-cash impairment charge that was included in our GAAP results. The majority of that charge relates to our industrial and infrastructure products segment. As we have previously and regularly reported, revenues and margins in this segment have declined due to a variety of factors, including but not limited to slower economic conditions, excess capacity and increased competition and the ongoing uncertainty of government funding for US transportation projects. While this impairment is a non-cash charge, it does provide an indicator of the near-term financial outlook for these related businesses that I'll describe when I explain our 2015 guidance. And most importantly, it provides a continuing reminder that future acquisitions must be rigorously reviewed and vetted by us. Frank will put some color on this point in his concluding remarks.

Next I'll talk about each of our two segments, starting with Slide 5, the Residential Products highlights. End market demand from residential housing markets was very strong this quarter. The majority of our residential revenue growth came from parcel and postal storage products, which were up more than 40% compared to 4Q 2013 and now comprise 35% of our residential products segment revenues compared to 25% in 2012. The primary demand driver is postal authority initiatives to have more mail delivered to centralized mail receptacles rather than more costly door-to-door deliveries. And we expect this initiative will span several years. This segment also had nearly 10 percentage points of revenue growth in sales of roofing related ventilation and accessories.

Turning to Slide 6, the residential products segment's specific P&L performance, this segment's fourth-quarter sales increased by double digits, nearly all organic unit volume, as I just detailed. Despite the unit volume growth, this segment was unable to leverage it into higher profitability. The major headwinds were led by continued production ramp-up costs to service the steep increase in demand for our postal products, also followed by higher raw material and freight costs that we absorbed.

The absence of profit leverage from the higher postal product volume largely stem from continuing challenges related to recruiting and training reliable, skilled employees across three shifts per day. We have confidence that once we get past the production ramp-up phase, this segment will recapture 100 basis points of margin improvement. And while we believe that the increased production capabilities also will position us to better serve the secular growth for postal products at higher returns.

Now, turning to Slide 7, our Industrial and Infrastructure Products highlights. This segment's fourth-quarter sales decreased, in line with our expectation, a decrease of 6% from the prior quarter a year ago. Inside that statistic is a 7 percentage point decrease in volume, weighted to lower volumes sold into bridge and highway construction projects. It also includes a small decrease in sales volume of grading and fabricated metal products to general industrial end markets.

Regarding the bridge and highway construction projects, Gibraltar's products are critically designed components to maintain functionality under changes in load, wind, temperature and seismic activity. And while demand in this market is significant, with a large percentage of US bridges deemed structurally deficient or functionally obsolete, federal and state transportation agencies and legislators continue to struggle for sources of financing. The current federal transportation appropriation extends funding through May of this year. As a result, the federally funded projects that have moved forward have tended to be relatively short in duration and smaller in terms of dollars. We're working hard to win our share of the available projects, but in 2014 and for the near-term, our order rates, backlog and revenues from transportation infrastructure projects will continue to reflect the challenging government funding environment.

Turning to Slide 8, the industrial infrastructure products segment specific P&L performance. Regarding its operating income, the industrial and infrastructure products segment's fourth-quarter adjusted operating income was lower. The largest unfavorable factors were inflationary costs we have absorbed and a less profitable mix. Looking forward in near-term, the top priority in this segment will be finding new and additional ways to optimize its cost structure for current market conditions.

Now, to our outlook for 2015 beginning with Slide 9. We're coming off a year of 4% revenue growth that came from secular demand for postal products which supported centralized mail delivery initiatives. Absent that higher demand for postal products, our 2014 consolidated sales were flat to 2013, as lower sales at the transportation infrastructure markets offset the small, single-digit gains we had in revenues for residential roofing-related products as well as a small increase in our grating and fabricated products sold into industrial markets. In 2015 compared to 2014, we do expect market conditions in residential housing to continue its slow improvement with industrial and transportation infrastructure markets being equivalent to 2014.

Regarding the residential products segment revenues growth in 2015, it will again be led by higher volume for postal products. And although reroofing activity in 2015 is expected to be equivalent to last year, we do expect our roofing-related products of attic ventilation and rain dispersion products can grow a bit higher in 2015 due to new accounts that we won during 2014.

Regarding revenues in our Industrial & Infrastructure Products segment, we expect 2015 to be nearly comparable to 2014. Our guidance contemplates no marked changes in order rates for transportation products and projects, figuring that new federal appropriations will be level funded. And concerning this segment's exposure to general industrial markets, approximately 20% of its orders come from energy related sectors. And we expect the lower cost of oil will dampen order rates in 2015.

And as an aside, one anecdotal reference is North American Rig counts which have decreased since the start of 2015 and are down more than 20% compared to this time last year as producers and oil service companies trim projects, staffing and CapEx. Based on these revenue assumptions with our residential segment up in modest single digits and our infrastructure and industrial segment matching last year, our numerical guidance for 2015 is outlined on Slide 10 titled "2015 Financial Guidance".

We do anticipate an increase in our profitability in 2015 compared to last year. Despite our conservative expectations for revenue growth, 2015 profit increases are expected from the incremental benefit of cost reductions we completed last year that are involving overhead staffing, sales channel adjustments, and a facility closure, plus the additional 2015 productivity initiatives and other actions that we are taking. With modest margin expansion on full-year consolidated sales growth, we expect adjusted earnings per share in 2015 to be in the range of $0.55 to $0.65 a share. And this compares to the adjusted 2014 earnings per share of $0.47.

And for those of you running models, we expect our unallocated corporate expense will approximate 2% of sales, our income tax rate around 38%, and CapEx spending in 2015 is targeted at $16 million, which is approximately $3 million below our depreciation expense.

Now Frank has concluding remarks which are summarized on Slide 11.

Frank Heard - *Gibraltar Industries, Inc. - CEO, Director*

Thank you, Ken. In light of the guidance that Ken just outlined, we're looking at 2015 as a transition year fueled by new leadership with new initiatives to drive sales, margins, earnings and returns. Some of these initiatives are underway and are factored into our guidance while others have not yet launched. These amount to significant but incremental improvements and we expect to see stronger results in 2015 because of them. At the same time, this year won't be the game-changing best-in-class performance that we are committed to delivering longer-term, especially given the market outlook that Ken just described.

At the start of our call, I mentioned that our strategy includes three areas -- operational excellence, portfolio management and the acquisition as strategic accelerators. Executing on this strategy means making thoughtful and efficient use of capital as it relates to our existing operations and future acquisitions, making sure that whatever decisions we make are going to be sustainable going forward. It also means higher expectations as it relates to the senior leadership team, the corresponding strategic and tactical plans, and our financial targets. Wrapped around that are higher standards of accountability for our leadership and a greater sense of urgency in the way we push change throughout the organization.

With effective leadership, even the best analytical and assessment work and the most thoughtful strategic planning will not alone allow us to achieve our goals. We've reviewed our existing businesses in supporting leadership teams in the context of not just who we are today but, more importantly, with a view to what we want Gibraltar to achieve in the future.

During the past six months, we've made key changes in our leadership at the business level across the Company while at the same time bringing complementary skill sets into the organization at the board, CEO, and senior leadership levels. We believe that, as a result, will further enhance our ability to meet and exceed our stated goals as they relate to driving long-term profitable growth and delivering a higher level of shareholder return.

Looking first at operational excellence, over the past few years, the Company has been very successful in rightsizing the various businesses in line with the size and health of their respective end markets. For the most part, these projects were designed in anticipation of a rebound in end market activity. But instead of rebounding, the majority of our end markets have continued to soften with a much more extended view as to when they will recover to past levels. This environment presents us with additional opportunities to rightsize and simplify the business and further enhance its profitability. To drive these initiatives, we're using the proven 80/20 process to focus our people, resources and capital on more attractive markets and our key customers and products. This should enable us to gradually and significantly improve the margin leverage in our business.

Driving out complexity in our existing portfolio is just step one. We also have to think differently about how we allocate people and capital, both inside and beyond today's portfolio. We're making good progress in the strategic review of our current businesses in the context of their market size, demographics, and relative profitability.

We are also taking a closer look at our ability to innovate and differentiate ourselves through the use of technology and have that translated to a higher level of shareholder return than in the past. We anticipate completing the review this quarter, which should position us to allocate our leadership time, capital, and resources to the platforms and businesses which we believe play the most critical role in our long-term success.

For example, we're working on some exciting products will expand and strengthen our postal and parcel storage platform. The developed nations globally are migrating from curbside to centralized delivery with all stakeholders struggling to resolve the high cost of securing the last mile. We have new solutions in the pipeline to address that growing need.

Elsewhere in the residential products segment, we are focusing on innovative technology that will allow us to leverage today's roof ventilation business into air management throughout the home. This will take us into markets beyond the replacement of roofing market and better align us with the growth in new single and multifamily housing starts.

The third dimension of our strategy, also underway, is to make more effective use of acquisitions. In the past, Gibraltar's approach to acquisitions was opportunistic, that is driven largely by ideas generated through the normal course of business. Our objective now is to be more proactive in pursuing new opportunities internally and in partnership with outside resources.

In the course of this strategic review that I just mentioned, we've identified a number of interesting opportunities in both products and markets. Rather than pursuing these opportunities based on their strategic fit with who we are today, we will be pursuing them with an eye towards the company we want Gibraltar to be in the future.

For example, we're excited about the opportunities in transportation infrastructure. Despite the short-term effects of the current funding environment, we believe the long-term prospects in this space remain attractive and see this as the key part of our financial future.

With activity in the infrastructure markets remaining depressed, some of the key players are considering divesting part of their business. We continue to target and entertain opportunities as they come available.

In addition, we've allocated dedicated resources to research and evaluate new platform opportunities based on innovative technologies that we can leverage with our core competencies in engineering, manufacturing, and distribution.

To support our acquisition strategy, we've instituted a much more disciplined approach to our prospecting in strategically important markets and product platforms, utilizing a more formal acquisition filter and supporting a financial model focusing on higher returns over a longer period of time. We expect this to result in greater alignment to our strategies and our desired portfolio mix, thus contributing to sustainable results over the long-term.

So, to summarize, our strategy includes three key areas -- operational excellence, portfolio management and acquisitions as the strategic accelerator. And we'll be discussing these areas and corresponding opportunities in greater detail at our investor day in New York City on March 26, which we hope you'll be able to attend in person or via the webcast.

Our overarching goal is to achieve best-in-class as it relates to sustainable wealth value creation and shareholder returns over the long-term. We look forward to reporting our progress and executing against this goal in 2015 as well as delivering improved financial results.

At this point, we'll open the call to any questions you may have at this time.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Ken Zener, KeyBanc Capital Markets.

Ken Zener - *KeyBanc Capital Markets - Analyst*

You know, since you're breaking your business up into residential and industrial, could you talk about the trends in residential that you saw were obviously very strong within your clusters, but could you give us a little sense of how that sales trend might look or the visibility you have for that business in 2015? Just so we can understand how you're kind of mid single-digit growth it sounds like it res will actually fall out. Is it going to be really lumpy as we try to understand the operating leverage in that business?

Ken Smith - *Gibraltar Industries, Inc. - SVP, CFO*

Ken, I think we have pretty good visibility. We do have an increase in backlog for that business platform, product platform, compared to a year ago. So even though it doesn't fill out the full year 2015's revenues, we think the underlying initiatives by postal authorities coupled with our backlog plus the ongoing replacement rates that have been pretty steady for the single mailboxes will fulfill the guidance that we've got for that platform embedded in our guidance.

Ken Zener - *KeyBanc Capital Markets - Analyst*

So are you guys talking about, I mean, if it's single digits, is it going to continue? Is it going to be stronger in the first half versus the back half? And the reason I'm asking that is your 100 basis point expansion corporate, I'm wondering if you can kind of give us a feel for how that 100 basis point EBIT expansion overall is going to play out within the segments, given that obviously the high growth you had in cluster was part of the drag that you had as you finished the year?

Ken Smith - *Gibraltar Industries, Inc. - SVP, CFO*

I'll start with a two-part answer to your question. One is we really stepped up the volume increases during 2014, beginning really in the second quarter of 2014. So our most distinguishing differential between 2015 and 2014 will be in the first three to four months of this year where we'll have that sustaining growth incrementally impacting essentially the first three or four months of 2015 to the strong degree that it did in 2014 over 2013, for example.

The second part of my answer is on the basis points. I do believe that the majority of our inefficiencies that we've been striving to drive out of the production of that product line will largely get behind us as we get into the beginning of the second quarter. So while I think that 100 basis points is an annualized number, I think we could capture a majority of that in this calendar year.

Frank Heard - *Gibraltar Industries, Inc. - CEO, Director*

I think, Ken -- Frank -- another point in that segment would be we had some facility relocations and integrations within the residential segment within our roofing ventilation business that I think we will see the benefits of that relocation and resulting cost reduction start to show up in the first quarter of 2015 into the second quarter.

Ken Zener - *KeyBanc Capital Markets - Analyst*

Okay. So when you're talking 100 basis points, I apologize if I missed it in your prepared remarks, but was that more -- the 100 basis points corporate, is that equal across the segments? It sounds like obviously the industrial is facing a lot more headwinds. So if you are doing flat growth in industrial, are you guys expecting flat EBIT in that segment as well?

Ken Smith - *Gibraltar Industries, Inc. - SVP, CFO*

My 100 basis points remark related to the residential products segment margin.

Ken Zener - *KeyBanc Capital Markets - Analyst*

Okay.

Ken Smith - *Gibraltar Industries, Inc. - SVP, CFO*

On an annualized basis, once we've got inefficiencies wrung out of the production, which I'm describing as being the front half of the second quarter this year.

Ken Zener - *KeyBanc Capital Markets - Analyst*

Okay. And if I could ask one last question, if you don't mind. The industrial, obviously with oil or energy at 20%, could you give us an update in February as it relates to the fourth-quarter results in terms of pricing at the service centers inventory? Thank you.

Ken Smith - *Gibraltar Industries, Inc. - SVP, CFO*

Well, raw material costs for steel continued to be volatile but declining as exiting -- as we finished up on the fourth quarter. And that's been a continuing trend into the front end of this first quarter.

So inventories I'd say generally were maintaining -- being maintained leanly because buyers were hoping that downward would continue and they could make subsequent purchases at even lower price points.

So part of my answer to you is that inventories continue to be lean, particularly for the purchasers of standard product of our bar grating equipment.

Frank Heard - *Gibraltar Industries, Inc. - CEO, Director*

I think, Ken, just to add to that, I think that applies to the general industrial side of our core AMICO business. I think how that falling price of oil affects that business is tied to the fabrication side where we have slightly higher margins because of some of the value-added processes we do when we sell into large projects into the oil and gas market in Continental United States and Canada. That backlog, because those are long-term projects, have not changed materially but I would suggest that depending on how long the price of oil continues to float in the range it is today will start to affect some of that capital spending in future years. These tend to be two-, three-, five-year cycles on some of the size and length of these projects. So we see that. We expect to see that new order book start to decline over the next 12 months.

Ken Zener - *KeyBanc Capital Markets - Analyst*

Thank you very much.

Frank Heard - *Gibraltar Industries, Inc. - CEO, Director*

You're quite welcome.

Operator

(Operator Instructions). At this time, we've reached the end of our question-and-answer session. I'll now turn the conference back over to Mr. Heard for any closing or additional remarks.

Frank Heard - *Gibraltar Industries, Inc. - CEO, Director*

Thanks, operator, and thank you, everyone, for joining us today. We hope to see many of you on March 26 at our investor day. If you'd like more information on the event, please call our investor relations firm Sharon Merrill at 617-542-5300. Thank you again. This concludes our call.

Operator

Ladies and gentlemen, thank you very much for your participation in today's conference call. You may now disconnect. Have a wonderful day.

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