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ROCK - Q1 2017 Gibraltar Industries Inc Earnings Call

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Gibraltar Industries First Quarter 2017 Earnings Conference Call. Today's call is being recorded and webcasted. My name is Audrey, and I will be your coordinator today. (Operator Instructions)

I will now turn the call over to David Calusdian from the company's Investor Relations firm, Sharon Merrill Associates. Please proceed.

David C. Calusdian - Sharon Merrill Associates, Inc. - President

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 first quarter performance. These slides are also posted to the company's website.

Please turn to Slide 2 in the presentation. The company's earnings press 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 press release and remarks this morning contain adjusted financial measures. Reconciliations of GAAP to adjusted financial measures have been appended to the earnings release.

On our call this morning is Gibraltar's Chief Executive Officer, Frank Heard; and Chief Financial Officer, Tim Murphy. At this point, I'll turn the call over to Frank, and please turn to Slide 3.

Frank G. Heard - Gibraltar Industries, Inc. - CEO, President and Director

Thanks, David. Good morning, everyone, and thank you for joining us on our call today. We began the year with a solid first quarter performance that came in just about as we anticipated. Business conditions for the quarter were generally in line with our expectations, and our top and bottom line results were within the high end of our guidance range.



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As we discussed on our last call, we entered the quarter facing some headwinds, namely lower backlog in our Renewable Energy, Industrial and Infrastructure segments and a difficult year-over-year comparison with Q1 2016 results as a result of exited businesses. And while raw material pricing also had an anticipated impact on results, we worked in close partnership with our key customers to mitigate these incremental costs.

On the positive side, strong demand for our centralized mail and Express Locker solutions, combined with solid performance from our ventilation and building products businesses, drove top line and margin growth in the Residential Products segment.

Looking at the high-level numbers for Gibraltar overall, Q1 consolidated revenues were down 13%, resulting in GAAP earnings of \$0.12 and adjusted earnings of \$0.20, landing at the high end of our guidance.

During the quarter, we continued to gain traction from our 4-pillar strategy, particularly in the areas of innovation and acquisitions. Our product development initiatives are gaining momentum, and we're very excited about our two most recent acquisitions, which are playing out as we had expected. I'll provide an update on our progress on each pillar later in the call.

But first, I'd like to take a moment to introduce our new Chief Financial Officer, Tim Murphy, who was previously the Vice President, Treasurer and Secretary of Gibraltar. He brings strong financial acumen, a deep understanding of Gibraltar's business drivers and a high level of strategic thinking to his new role. I also want to thank Ken for his dedication and contributions during his 9-year tenure as CFO for Gibraltar. Ken, on behalf of Gibraltar -- of the Gibraltar team, our shareholders and the board, we wish you all the best in retirement.

I'll speak more about the traction we've gained with our 4-pillar strategy and provide guidance after Tim reviews our financials. Tim?

Timothy F. Murphy - *Gibraltar Industries, Inc. - CFO and SVP*

Thank you, Frank, and good morning, everyone. Let's move to Slide 4 on the presentation, entitled Consolidated Results.

Overall, we reported solid Q1 with both the top and bottom lines within our guidance for the quarter. This expected performance was against the backdrop of the headwinds that Frank mentioned earlier and that we discussed on our last call. These challenges were partially offset by strong demand for our Residential Products, particularly our centralized mail and Express Locker solutions.

As expected, revenues declined 13% compared to the first quarter of 2016, driven by a 12% decline from portfolio management actions we took during 2016. Base revenues, excluding the divestitures and the impact of acquisitions, were down 5%, which was in line with our expectation. The decline in base revenue was partially offset by revenue from our recent acquisitions. While not shown on the slide, gross margin increased 100 basis points from 22.8% in the first quarter of 2016 to 23.8% this quarter, which provides evidence of the value of the 80/20 process and the portfolio management actions taken during the previous 12 months.

As anticipated, in addition to lower volume, our bottom line was negatively affected by increased material costs and equity compensation costs that we were not able to cover within the 80/20 benefits realized during the quarter. While our portfolio management actions created a difficult year-over-year revenue comparison and resulted in a \$3 million charge during the quarter, we expect to see a positive effect on margins, reduced investment in working capital, fixed assets and overhead and an improvement in total return on capital from those product line exits. Overall, we delivered results as guided, and we saw backlog recover in our Renewable Energy & Conservation business, which now exceeds levels at the end of the year - prior first quarter.

Next, let's talk about each of our three reporting segments starting with Slide 5, the Residential Products segment. Strong demand for our centralized mail and Express Locker solutions, along with a \$600,000 contribution from our Package Concierge acquisition drove the increase in sales for the quarter. Revenues also benefited from pricing adjustments and the gradual improvement in the new construction and repair/remodeling activity. On the bottom line, we benefited from the continued effects of operational efficiencies via 80/20 simplification.



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Turning to Slide 6, the Industrial & Infrastructure Products segment. Segment revenues were affected primarily by the exits of the U.S. bar grating and European industrial businesses, which accounted for \$27 million of the decline. The remainder of the decline in revenue in this segment is a result of a year-over-year sales reduction in our infrastructure business.

After announcing in December of 2016 that we would be exiting the U.S. bar grating business, we were able to sell substantially all of our U.S. bar grating assets during the first quarter. We were very pleased to provide the opportunity for continued employment to a substantial number of our highly skilled employees and with the timing of liquidation of the assets we had invested in this business. We continue to manufacture and distribute expanded metal, plank grating, lath and trim, along with perimeter security solutions to our customers in North America. We remain committed to providing our customers with best-in-class service as we advance our strategy to focus our resources on the highest-return markets, platforms and businesses.

On the infrastructure side, sales were down about 14% as we entered the quarter with lower backlog than the prior year, partially due to a large project we completed for a customer in the energy space in 2016 and partially due to lower bridge repair activity in 2017. We continue to see delays for infrastructure products, with only a modest increase in backlog in the quarter. However, bidding activity is picking up, and our hit rates remain consistent. And this activity is in line with the expectations we had as we entered the year.

On the bottom line, in addition to the sales decline, industrial margins were pressured by increases in raw materials, and we expect to continue to see this pressure during the second quarter impacting both sales and earnings. Nonetheless, with the Industrial & Infrastructure team's aggressive application of 80/20 projects and the lessening impact from material cost price alignment, we expect improved profitability for this segment in the second half of 2017.

Now turning to Slide 7, the Renewable Energy & Conservation segment. Revenues in this segment were impacted by lower backlog entering 2017, both domestically and internationally. Our greenhouse business continues to perform, and our Nexus acquisition provides additional opportunities for growth. We're integrating Nexus and refocusing both the RBL greenhouse business and Nexus to capitalize on new high-growth markets.

We are seeing backlog grow, up almost 32% during the quarter, with backlog at this business exceeding the level it was at, at the end of the first quarter of 2016. We are experiencing softness in orders in our international renewables business, and it is anticipated to cause a year-over-year reduction in sales of approximately 5% in the renewable space. And we expect to make up that shortfall in our international business with continued growth domestically. With our continued sharing of our design-based cost reduction with our renewable customers, we expect domestic sales in the second quarter to equal prior year levels, with domestic sales growing from the second half of the year.

On the bottom line, profitability was affected by the lower volume, price reductions we shared with our customers, the cost benefits we realized from our product redesign and 80/20 activities in the prior year and higher material costs. We accept -- expect these same factors will impact the second quarter, and our sharing of the cost reductions with our customers will remain evident through the year. Overall, we expect top and bottom line growth in our domestic renewables business in the second half of the year as we begin to fulfill the strong orders we have in backlog.

Please turn to Slide 8, Capturing the Opportunity. As you can see from the slide, we continue to have low leverage and high liquidity, which puts us in an excellent position to execute on our acquisition strategy. We used \$9.3 million during the first quarter as the cash generated from our operations and proceeds from the sale of our U.S. bar grating business partially offset the \$18.6 million we spent on the acquisition of Package Concierge.

Acquisitions will continue to be a priority for 2017. For the past year, we've been targeting companies with approximately \$25 million EBITDA. However, with our strong balance sheet and significant liquidity, we've expanded our focus to include businesses between \$50 million and \$100 million in EBITDA. That said, there are still smaller acquisitions that could be beneficial from a technology standpoint. Going forward in 2017, our financial priorities will be to drive sales through innovative products, seek value-added acquisitions in attractive end markets, create additional benefits from our 80/20 initiative, effectively manage pricing against the backdrop of higher raw material costs, and in the end, making more money at a higher rate of return with a more efficient use of capital.



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At this point, I'll turn the call back to Frank, who will review the progress in our 4-pillar strategy and our guidance going forward. Please turn to Slide 9, "4 Pillars Driving Value Creation." Frank?

Frank G. Heard - Gibraltar Industries, Inc. - CEO, President and Director

Thank you, Tim. Our four-pillar value creation strategy continues to gain traction and deliver results. In our first pillar of "operational excellence," where our focus is on reducing complexity, adjusting costs and simplifying our product offering through the 80/20 initiative, we continue to see benefits from projects started in 2016, with savings of \$2 million or \$0.04 per share achieved during the first quarter, and we're on track to deliver the expected \$0.21 per share increase from the implementation of these projects in 2017.

We also expect to see the acceleration of the in-lining of our manufacturing processes, which is the foundation for implementing market-rate-of-demand replenishment and the resulting make-versus-buy decisions as the year progresses. During the quarter, we regard -- reviewed four key projects related to in-lining, and our teams are planning for the necessary physical changes as the year progresses. All is going according to plan with this effort to date.

In "portfolio management," where we evaluate product lines, customers and end markets to best allocate leadership time and resources to the highest potential platforms and businesses, our planned actions were essentially completed at the end of 2016. This included the exit of three platforms, two in our industrial segment; and the third one, our European solar racking business that served the residential rooftop market. During the past quarter, we continued to wind down the last pieces of these exited businesses. At the same time, we're enthusiastic about the businesses that remain in our portfolio in these areas. For example, our team at Amico is working on some very innovative products that should provide us with good growth prospects in 2017 and beyond.

This leads me to our third pillar, "innovation." We define innovative products as those with patent protection, driven by internal product development or acquired product lines. And in 2017, all of our segments were actively working on this initiative.

In our Residential Products segment, our Express Locker centralized parcel storage product continues to experience strong demand. The acquisition of Package Concierge, which is the front end of our Electronic Parcel Locker solution and a leading provider of technology, will allow us to accelerate our growth in the multifamily market in both the Class A and Class B segments. In our residential roof-related products, our new metal roofing installation system that can withstand hurricane force winds is moving forward in development and related approvals, and we're on track to realize our first sales in the second half of this year.

We're also advancing our perimeter security products developed in our Industrial business, capitalizing on increasing demand for solutions to protect high-value physical assets. We introduced our new perimeter security solution last September, and during this quarter, we began the bidding process for multiple contracts in the utility and infrastructure markets. We continue to expect this product to contribute to both top and bottom line growth in 2017 and beyond.

In Renewable Energy & Conservation, we're focused on expanding market share with new products, targeting spaces adjacent to its core ground-mounting racking systems. And during the quarter, our new products advanced from preliminary development into final testing approvals, and we're working on the necessary supply chain initiatives for a launch before the end of the year.

Innovation is a key part of our filter in evaluating acquisition opportunities, which is our fourth pillar. During the quarter, we acquired Package Concierge in our Residential Products segment. Package Concierge is a clear market leader in the multifamily segment, and through this acquisition, we plan to accelerate our presence in the overall fast-growing Package Delivery Locker market. PC's proprietary software solution and deep understanding of the multifamily market coupled with our current Express Locker product provide Gibraltar with a distinct competitive advantage. In fact, the synergies between the residential segment and Package Concierge open a market that's 5x larger than the one we currently participate in, in the single and centralized mail. This acquisition follows the fourth quarter acquisition of Nexus in our Renewable Energy & Conservation market.



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With RBI and Nexus working together, we're now well positioned to accelerate our growth in the conservation markets as it relates to both the commercial greenhouse segment and the rapidly growing medical marijuana market. Nexus has been accretive since the date of acquisition, and we expect that PC will continue our bottom line -- continue to contribute to our bottom line starting in 2018 while driving a higher level of volume and profitability in our core electronic locker business in 2017. With a rapidly improving balance sheet, we remain focused on prospects that participate in attractive end markets, with opportunities to improve market share and drive operational enhancements while solving [problems] for real end users and related channel partners.

Turning to Slide 10, "2017 Guidance." For 2017, we continue to expect to generally -- expect generally favorable market conditions, aiding top line growth for our Residential segment. All 3 of our segments are working to expand into adjacent product categories and applications, and we expect these efforts to contribute incrementally to 2017 sales.

At the same time, we expect consolidated results to be challenged by difficult comparisons to 2016 as a result of our portfolio management actions to drive higher profitability and returns, a slower recovery in Renewable Energy & Conservation segment as we continue to rebuild our order book from the lower order rates we experienced in the back end of 2016 combined with difficult market conditions in the industrial and infrastructure markets and higher-than-expected raw material pricing. While we believe these factors will result in lower year-over-year top-line and bottom-line results for the second quarter, we expect a return to earnings growth during the third and fourth quarters as we capitalize on improving demand in Renewable Energy & Conservation, where our backlog exceeded prior year levels at the end of the first quarter, combined with benefits from our recent portfolio management and product innovation actions and the expected effect of declining raw material costs.

For the second quarter, we expect revenues will be in the range of \$249 million to \$254 million compared to base revenues of \$251 million in the second quarter of 2016. The lower sales volume, coupled with higher commodity costs, will result in GAAP EPS between \$0.35 and \$0.40 per diluted share or \$0.37 to \$0.42 on an adjusted basis.

As a result, we're revising our full year guidance. In light of the factors I just mentioned, we now expect 2017 sales in the range of \$970 million to \$980 million, a 3% growth in base revenues, with GAAP EPS between \$1.37 and \$1.50 per diluted share or \$1.57 to \$1.70 on an adjusted basis. Looking at the remainder of 2017, we expect to deliver a third consecutive year of solid financial improvement on a GAAP basis in terms of absolute profit dollars, returns and cash flow.

In conclusion, we remain confident in our value-creation strategy and are taking the appropriate actions to build sustainable long-term value for our shareholders. We're seeing significant progress within each one of our four pillars, and we're very excited about Gibraltar's future going forward.

At this point, we'll open the call up for any questions you may have. Thank you.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of Daniel Moore with CJS Securities.

Daniel Joseph Moore - CJS Securities, Inc. - MD of Research

I wanted to just parse out a little bit the sort of updated guide and the implications for H2. Maybe talk about your -- obviously, backlog is up a little, but talk about the factors that drive your confidence in renewables returning to growth or reaccelerating as well as your visibility. And a quick follow-up or 2 there.



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Frank G. Heard - Gibraltar Industries, Inc. - CEO, President and Director

Sure. Tim, do you want to...

Timothy F. Murphy - Gibraltar Industries, Inc. - CFO and SVP

Yes. Let me -- Dan, let me give you a little background. I guess a lot of our confidence is driven by our customer discussions. Our customers are generally telling us that they're going to install more solar this year than they did last year. We're seeing bidding activity at greater levels than last year, and our hit rates remain consistent. The reason that we have a little pause in our sales forecast certainly in the second quarter and then drifting into the second half of the year is that we're seeing lead times a little bit longer than we have historically. We think that's driven by a lack of a hard ITC credit stop, and so projects are just taking a little bit longer from when we sign the contract to when we can complete them.

Frank G. Heard - Gibraltar Industries, Inc. - CEO, President and Director

Yes. And I think Tim's point -- opening point around our customer interaction, we have very strong partnerships. As, Dan, you know, we're focused on kind of ground mount fixed and we're about 1/3 of the market there. And our value proposition is quite unique in that we do from project design all the way to install, unlike our competitors. So we have a strong connection. So we created a little bit of a flat spot for a quarter that we expected in the first quarter simply because we drove an awful lot of profitability through the investment of introducing new roll formers and raw material sourcing. And we've kind of suppressed the top end for the back end of 2016 a little bit in order to let the supply side catch up in terms of the implementation of those three roll formers once a quarter to then take advantage of being able to sell a more cost-effective racking solution. So we expected a flat spot in the first quarter. But I think Tim's added point about as we've gone back out to integrate -- to chat with our key customer base, we've got a rising backlog, we've got an increase in bidding activity, our customers expect stronger numbers this year than last year. So we're feeling pretty confident that the back end is similar to some of the prior years that RBI experienced as they entered the market prior to us acquiring them and that hard stop -- or that full stop at the end of 2015 that created some confusion in the market. So I think we're getting back to a stable market. And the third-party outside reports, outside of residential, outside of tracker, outside of commercial rooftop, suggest 5% to 7% top line growth in the fixed-tilt market that we participate in. And that's what we kind of expect to experience going forward. So we take out the international piece, which is a little bit of a headwind for us, that's consolidated in these numbers and our core business in North America look strong going forward. So we're feeling very good about it.

Daniel Joseph Moore - CJS Securities, Inc. - MD of Research

Helpful. Another component of that guide was raw material. Maybe just, if you can quantify the impact of rising raw material prices in Q1. And then you expect that to lessen, is that based on price increases that you're putting in? Or you're expecting raw material prices to decline as we go through the back half of the year?

Timothy F. Murphy - Gibraltar Industries, Inc. - CFO and SVP

Dan, we experienced about \$2 million of raw material price cost misalignment, let's say, in the first quarter. We started the year expecting about \$0.12, if you go to a bridge on Slide 11. We've increased that by \$0.04 as we see some more of that coming through mainly in our I&I business in the second quarter, and then we expect it to moderate.

It doesn't -- we have to go to customers and work with them so we're seeing price adjustments. And we're also seeing steel costs come down in the marketplace. So the combination of those two give us confidence that, as we look through the second quarter, it'll be pretty close to neutral for the rest of the year.



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Frank G. Heard - *Gibraltar Industries, Inc. - CEO, President and Director*

Yes. And I think that kind of -- the second quarter impact of that before we kind of see the effective - it takes the quarter of the impact to kind of implement the pricing and then get those adjustments as best you can and we work with our key customer partners on that. I think the other side is, we're now seeing hard numbers where our raw material input costs going forward are coming down. To some degree, we've got a quarter of adjustment on both because we're carrying inventory at those higher costs. It's going to take us 60 to 90 days to burn through before we get the benefit of the lower material prices going forward. So it's kind of a quarter of transition that's built into our second quarter guidance.

Daniel Joseph Moore - *CJS Securities, Inc. - MD of Research*

Perfect. And lastly, and I'll jump back in queue, but the third component of the expected increase in H2 is a little bit of an industrial recovery and just talk maybe a little bit more color on what you're seeing there.

Timothy F. Murphy - *Gibraltar Industries, Inc. - CFO and SVP*

Our industrial business, what's left is a strong business, and randomly some headwinds with material. We're going to have some material headwinds in the second quarter. But as they sit with their customers, the customer's demand is -- it's not growing at 10%, double digits, but it's low-single digits and we're participating in the markets. We're happy with the relationships we have. We've got new products launched in that place in perimeter security that are starting to get some traction. We expect more of that in the second half than in the second quarter, but we're seeing it come through during the quarter.

Frank G. Heard - *Gibraltar Industries, Inc. - CEO, President and Director*

Yes. And certainly, to our portfolio management actions exiting bar grating, exiting Europe, we really feel strong with what we have as a core group of businesses within the AMICO Industrial Group now. And while they're doing some tremendous work on 80/20 in the first year to drive margin enhancements and the portfolio management in the second year, early in 2016, we really start to focus in on the perimeter security market where we've always participated with a small product line that if you go way back, it actually help build part of the original wall between U.S. and Mexico. And as we've researched that industry segment, we realized it's the -- with the changing world, it's a very significant rising tide. It's over \$1 billion market opportunity in the U.S., probably somewhere around \$2 billion globally, and growing at high single digit CAGRs with some real technology products. Not just fencing-related product only. So our guys have really spent the big part of 2016, while they're doing some difficult work, also refining designs, filing for new patents to have both the renovation base security product, but new build product and they're are working on some very significant opportunities in terms of some of the larger players in continental United States, in terms of future contracts that could really help transform this business, beginning in the back-end of 2017 going forward in future years.

So we're pretty excited about the work they're doing. And we think this is going to be a key linchpin for why AMICO is going to be an important part of our portfolio going forward.

Operator

Our next question comes from the line of Walter Liptak with Seaport Global Securities.

Walter Scott Liptak - *Seaport Global Securities LLC, Research Division - MD of Diversified Industrials and Senior Industrials Analyst*

Just to follow up on that first question. The \$2 million of raw (material) price cost. Was that all in I&I? Or was there some in other segments as well?



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Timothy F. Murphy - *Gibraltar Industries, Inc. - CFO and SVP*

It's mixed. There's a little bit, as you'll recall, in renewables. We did some price adjustments at the end of last year. So some of that would flow through there, but I would say that I&I is the largest piece.

Walter Scott Liptak - *Seaport Global Securities LLC, Research Division - MD of Diversified Industrials and Senior Industrials Analyst*

Okay, great. And then just to maybe dig a little bit deeper into the renewables part of the business. I think you've just had great success so far with portfolio management and thinking about what's going to grow, what's not going to grow. And I think the solar business that's a little bit lumpier than maybe some of the other businesses that you currently have. And I wonder, what you think about still longer term in this business? Obviously, you're making investments into some new products. Is this an area that you'd be continuing to look for acquisitions?

Frank G. Heard - *Gibraltar Industries, Inc. - CEO, President and Director*

Yes. We're certainly -- there's four end markets, we participate in one. We think you know there's commercial rooftop, residential rooftop and sort of the larger tracker space. Some are more similar to what we already do than others. But certainly, two out of the other three, we would have interest in and we've been looking at various opportunities to enter those spaces since we bought the original RBI business.

Our view of the market hasn't changed very much. It's high single digits CAGR going forward. By and large, all four segments are pretty close to grid parity now in terms of cost. So we've been -- based on what we've been able to do in terms of some of the synergies, we know we can make high-teen kind of margins in the space, and we can dominate some, with some fairly significant share and unique product solutions. So if the right opportunity came along and we've looked, then we'd certainly put more money to work in that space.

And in the meantime, we're spending an awful lot of time working on it from an organic product development perspective. And in the absence of an acquisition, feel pretty good about our progress and its potential impact in the back end of '17 going forward into '18. So no reservations about our investment today. In actual fact, we're way ahead of our expectations in terms of financial returns.

Walter Scott Liptak - *Seaport Global Securities LLC, Research Division - MD of Diversified Industrials and Senior Industrials Analyst*

Okay. The bookings that you took in this quarter, do those all ship in the back half of 2017? Are those -- some of those push into 2018? And what's the -- I think you kind of alluded to some of this already, but what are chances that we see more slippage of projects further into the fourth quarter, into 2018 as we see more volatility in that Renewable segment?

Timothy F. Murphy - *Gibraltar Industries, Inc. - CFO and SVP*

Based on what on what we know today, based on our conversations with our customers, based on the orders we have and the schedules that they're at, we think we got it in the right period. So to see wholesales slippage would be a surprise as we sit here today.

Frank G. Heard - *Gibraltar Industries, Inc. - CEO, President and Director*

Yes. And -- well, in fact -- I just want to clarify. I don't think that we're seeing a lot of volatility per se. I think what we're seeing is kind of the first full year settling out of what normal demand would look like in this particular space, which is forecast in the 7% range, and it's adjusting out for some of those artificial deadlines that were put in place through a forecast closure of ITC and people are now settling into kind of what normal demand would be without any false lines in the sand in terms of getting credits and so on and so forth.



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So the -- unless there's -- and there's some political climate change where it created some uneasiness as well. That's come and gone. So I think we're back, the market's back to expecting the last extension of the ITC going out through 2020. That would mean what the expected marketing conditions they have to operate in.

So I think that's -- our view of it is that we're starting to see the dust settle a little bit and people are getting back to what normal demand look should be. So it's our expectation that the backlog, the growing backlog position we have and the feedback we're getting from our customers and the senior management in that group is that the lion share of that will be reflected in 2017.

Walter Scott Liptak - *Seaport Global Securities LLC, Research Division - MD of Diversified Industrials and Senior Industrials Analyst*

Okay, fair enough. Just a follow-on to that, then I'll get back in queue. The new products, you alluded to, or you -- it sounds like you're pretty far along with the final testing, supply chain. Can you give us an idea of the market opportunity for the new renewable products?

Frank G. Heard - *Gibraltar Industries, Inc. - CEO, President and Director*

It's -- we try not to go too far because at this stage, it's certainly material in the context of the business space we're in today, and we think we could be disruptive. We don't want to go too far at this stage until we're kind of fully in the market launch. We do have a competitive landscape out there. So at this stage, we're not to go any deeper with detail.

Operator

(Operator Instructions) Our next question comes from the line of Ken Zener with KeyBanc Capital Markets.

Kenneth Robinson Zener - *KeyBanc Capital Markets Inc., Research Division - Director and Equity Research Analyst*

I have a lot of questions for you on solar. Some of these I've raised with you in the past. But I -- it's going to be about the visibility related to margins, more than sales, actually. So I'm going to -- it's going to be a little set of questions here. Well, I understand the macro backdrop for the ground mount that we addressed in a recent note.

If you could kind of talk about a little more explicitly, the margin confidence factors that you have and going to be related several key factors. So if you have a pencil, Tim or Frank, that will be helpful, actually. And I apologize.

But first, your backlog duration, I believe it's less than a quarter, so what is that? Second, related to the margins. You say you're sharing price with customers. And what does that kind of mean versus, I think you kind of talked about a 15% EBIT rate last quarter plus the quarter before when you had the revisions. So and -- where does that comment come from if your backlog not going into the back half? And then the third component is, can you talk to the backlog margins for what you have today? And what percent of 2Q, for example, revenue, is there? Per share guidance in 2Q in second half? And if you could kind of be explicit around those EBIT margins, that will be useful.

And what does that mean for kind of the contract purchase price agreements? Or is there a relationship between the PPAs that are out there in the market now as people like yourselves are sharing some of this price? And how does it relate to the PPA that's out there? That's one large question, I realize.

Timothy F. Murphy - *Gibraltar Industries, Inc. - CFO and SVP*

Yes. All right. So let me start. Backlog duration. Yes, I mean, a quarter, 90 days is maybe what we had experienced. We think it's a little bit longer now, because we're seeing a bit of a shift of when the customers what the work done from when they sign. So we might have some of the stuff in



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backlog today that will drift into the third quarter. And that's it. It [isn't] perfect because sometimes you have something that's not going to shift for 9 months.

But in general, I think, maybe a about a month in the shift, is what we're seeing. When we share price with customers, so last year, after we completed putting manufacturing in-house and growing out our new design, we realized we're even more efficient at manufacturing than we have planned. And so we really had greater savings than we anticipated. And so thoughtfully, in the fourth quarter, we started to share that with customers. And so I think last year, we ended within the 17% operating margin range for that business and we said that longer term, we think, should be around 15%, give or take.

So then, I think the second half of your question, how does that impact second quarter and then rest of the year. And I guess, I would describe second quarter, the pricing and backlog is consistent with that, but we have a little bit -- we still have a little bit of volume shortfall in the second quarter in that business. And I think in the remainder of the year, from where we stand, we think we're back into that -- into the respective range for that business. Then you asked about . . .

Kenneth Robinson Zener - *KeyBanc Capital Markets Inc., Research Division - Director and Equity Research Analyst*

Sequentially? Tim, would that be sequentially equal with first quarter then? Or would that push higher with a bit of a volume driver? I'm just thinking fundamentals...

Timothy F. Murphy - *Gibraltar Industries, Inc. - CFO and SVP*

Yes. Yes. It's improving. But it's just not all the way there yet because the volumes is still...

Frank G. Heard - *Gibraltar Industries, Inc. - CEO, President and Director*

And I think the other thing that will impact, suppress the second quarter little bit is, like in the other segments, even though we made significant progress and -- on the raw material sourcing work that we did for RBI, like in the other businesses, we took proportional increases in raw material that we're also seeing subside but we've got inventories that we're going to have to burn through in the second quarter that would have some impact on that margin as well. That would start to relive itself as we go forward in the third and fourth quarters as well.

So, all that being said, we bought a -- close to a 9% business and as Tim pointed out for a variety of set of circumstances and a lot of good work we ended up in 17%, we don't see those kinds of margins in that industry. We see this kind of 10% and below. But we do believe that we've got something unique, that's why we bought it. And we do think that on a sustainable basis, that we could be mid-teens with very light capital investment, so some very significant returns from a return on invested capital.

We're not -- we think we're given away the appropriate amount going forward. We think we got a unique cost base and value proposition that gives us a little bit of a premium versus competitors and we're not uncomfortable about thinking that we can maintain a 15% return for the type of share that we're looking for, which is about a 30% to 35% of the market in that segment.

Kenneth Robinson Zener - *KeyBanc Capital Markets Inc., Research Division - Director and Equity Research Analyst*

Okay. So it sounds like the -- it might be 10%, it might be kind of 13% in the back half. And I ask -- realizing there's a lot of macro factors and I do believe that you guys are executing on what you could control well. I guess, this obviously is critical, Frank, to the story because given the momentum that you've had, this is the first time we've seen kind of an air pocket, if you will. I know you guys are going to be hosting a solar kind of event in a few weeks, correct?



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Timothy F. Murphy - *Gibraltar Industries, Inc. - CFO and SVP*

Yes, we are.

Kenneth Robinson Zener - *KeyBanc Capital Markets Inc., Research Division - Director and Equity Research Analyst*

I guess, one of the things, given that this business is central, I think, to your stock, from an earnings basis, but also the multiple, right? So when investors are going to ascribe to your business in terms of the consistency and the valuation level. I'm not sure if how you guys are going to be filtering what your, the message that you're going to be communicating if you're going to be doing it publicly -- to the extent that you can be sharing as much as is happening there? Broadly, with the events, I think that would be very helpful because there's so many different questions, for example, like the PPA. I mean, I understand the margins, but -- or purchase price agreements, the deflation on that is -- how is that impacting you, for example?

Timothy F. Murphy - *Gibraltar Industries, Inc. - CFO and SVP*

Yes, I can answer that question. So I think every year, in solar, for the last however many years it has been, the cost comes down every year. And so we work every year with our customers to help them with their -- balance their systems cost. Part of what drives that cost is the cost per watt. So more efficient panels, drive down costs per watt without any reduction in price of anything, you just get more power from the same space. We do have a ground mount 3.0 rolling out. So last year, we rolled out 2.0, it's a design that reduced our cost and still met all the needs, we've got some additional tweaks that are coming out this year.

So that's a constant presence in that business to continually engineer our costs and work with our customers to get more watts for the same piece of metal that's on the ground.

Frank G. Heard - *Gibraltar Industries, Inc. - CEO, President and Director*

Yes. And just to support that. When we bought into this space, we did an awful lot of modeling on what we felt those future costs would look like. That as it related to ultimately getting down to grid parity, as it related competitive systems and whether be coal or nuclear or gas. The industry as it relates to whether it's wind or solar is pretty much a grid parity in most of the large states in Continental United States. So it's not like hey, we're going to continue down this path as a collective group whether with panel manufacturers or the balance with system segments where we participate.

We're down to kind of the last 10% or 15% of refinement on tweaking of cost and systems. And the reality is, we, as an industry, are already a better investment choice than the competitive alternatives, regardless of policy, more than 50% of new investment in energy production, in fact now in the United States comes out of renewals, and its largest employer in the sector. So it's not like there's this overweighting every time we have to -- we save a (dollar), we have to give away \$0.90 of it. I mean, those days are way past us. And when we're -- we did this modeling, we did a lot of homework in the future because we didn't want to buy in a space that was a rising tide but ultimately had declining profitability that ultimately, would be commoditized margins at 4% or 5%, which is what we're trying to, over the last couple of years, move away from.

So we're still pretty confident that we bought in the right space, it's a rising tide, we think we've got technology and we've got cost reductions that we've taken out, we've got more to come in terms of our systems, and we've got a great opportunity to get incremental volume leverage with new and innovative products that we're going to introduce later on in the year, so -- with a very low investment profile.

So, we like the space, we put more money to work. But from a portfolio construction, to go to one of your earlier point, our expectation is, we expect this roof to grow. But we also don't expect it to continue to be the only 50% of our weighting, from an EPS perspective, we've got a strong balance sheet, we're a couple of acquisitions away from having the right mix in terms of end markets. And having the right mix in terms of weighting, in terms of relative size of businesses within the portfolio.



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So we're not finished yet. We're halfway through our transformation. We don't view this as -- our commitment was over a 5-year period, we're working our way through it. And most of the execution of the 4 pillars has taken place as expected, with better than expected results. And I would argue that the only one we're a little bit behind on is, finding the next thoughtful acquisition in the right space that would have been accretive short-term but also long-term value creation similar to what RBI has provided.

Operator

At this time, we have reached the end of the Q&A session. I will now turn the conference back over to Mr. Heard for any closing or additional remarks.

Frank G. Heard - Gibraltar Industries, Inc. - CEO, President and Director

Thank you, everyone, for joining us on the call today, and we'll speak to you soon.

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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