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EDITED TRANSCRIPT

ROCK - Q4 2016 Gibraltar Industries Inc Earnings Call

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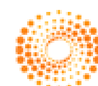

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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the Gibraltar Industries fourth-quarter 2016 earnings conference call.

(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 Calusdian - *Sharon Merrill Associates - IR*

Good morning, everyone, and thank you for joining us. If you've not received a copy of the earnings press release that was issued this morning, you can find 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 and full-year performance. These slides also are 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 are Gibraltar's Chief Executive Officer, Frank Heard; and Chief Financial Officer, Ken Smith. At this point, I'll turn the call over to Frank, and please turn to slide 3.

Frank Heard - *Gibraltar Industries Inc - CEO*

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

2016 was another successful year for Gibraltar. We achieved excellent financial results and executed well on all four pillars underpinning our strategy, and we are continuing to drive the sustainable transformation of the business. Since we laid out our strategy two years ago, we've made more money each quarter at a higher rate of return with a more efficient use of capital. And as slide 3 represents, the fourth quarter was very solid, noting

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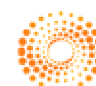

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the favorable comparison of adjusted EPS to prior-year's quarter, and the $0.30 per share also exceeded our guidance. The increase in adjusted profitability continues to be the result of the operational excellence initiatives within all of our operating units.

While not shown on this slide, our full-year 2016 results were meaningfully higher than 2015 in several key financial measures: gross margin, operating margin, EPS, both GAAP and adjusted, cash flow from operations and return on invested capital. And in addition to margins and returns improving, I want to use slide 4, entitled "Base Revenue", to point out that our base revenues also have been increasing. In prior quarters, we did not distinguish revenues affected by many proactive changes that we've made to our portfolio. Slide 4 draws from the appendix slides 18 and 19, where we isolated the non-recurring portions. For example, divested businesses, exit from product lines, and completed but discrete contracts; and then compared the remaining base revenues year to year. On slide 4, in each of the four squares, the darkest blue colored portion of each bar represents the base revenues and provides a better apples-to-apples comparison of our ongoing revenue streams. And in 2016, we have had base revenue growth compared to 2015 in two segments, and the Company's consolidated base revenues rose 4% as compared to 2015.

I'll speak more about our strategic direction, 2017 guidance, and the future initiatives after Ken reviews our fourth-quarter financials. Ken?

Ken Smith - *Gibraltar Industries Inc - CFO*

Thank you, Frank, and good morning, everyone.

Let's move to slide 5 in the presentation entitled "Consolidated Profitability Rises". Starting with the reported revenues on the slide, the unfavorable revenue comparisons were expected, as Frank just detailed. And these amounts include all historical sources, including from products and contracts we have or are exiting. Nonetheless, we continue to have strong bottom-line performance. On the bottom half of slide 5, specifically the bottom row, reports our adjusted results for the quarter and annual periods, and both were strong. And, reflect the benefits of many 80/20 simplification projects, as well as other separate cost-reduction actions. Although not shown on slide 5, the Company's consolidated gross margin improved at least 500 basis points over 2015, for the fourth quarter, the full year, and in both GAAP and adjusted measures.

The consolidated results reflect strong improvement by two of our three segments, the Residential Products and Renewable Energy and Conservation segments; while our Industrial & Infrastructure segment has continued to deal with significant headwinds related to lower order activity from commodity and oil and gas markets, which in part influenced our decisions to trim certain of its product lines. Overall, we feel we've established a good balance between growing our businesses and thoughtfully trimming the portfolio, resulting in the right formula to make more money at a higher rate of return.

Next I'll talk about each of our three reporting segments, starting with slide 6, the Residential Products segment. The reported revenues for this segment decreased, due to a two-year sales contract for centralized mailboxes that we successfully completed in December of 2015. However, aside from that contract completion, this segment has continued to see steady demand for its Residential Products, largely in line with a gradual improvement in new construction and repair and remodeling activity. Impressively, this segment's employees have also excelled in driving improved operational efficiencies via 80/20 simplification. On the lower right corner of slide 6, the operating margin comparisons, GAAP and adjusted, fourth quarter and full year, have each expanded by at least 500 basis points in one year.

Turning to slide 7, the Industrial & Infrastructure Products segment. In every section of this slide, as expected, its reports on a difficult year. This segment's exposure to the commodity markets and oil and gas have been a significant headwind for the last two years, and these particular markets purchased a meaningful portion of our bar grating product. Remarkably though, this segment's leaders and employees have been dealing effectively with it. For us, seeing the resiliency of its full-year operating margin, given the significant drop in order rates and related revenues, is very impressive, made possible by their aggressive application of 80/20 projects and other countermeasures. Additionally, we supported this team's recommendations to make meaningful adjustments to its product portfolio. Its only European industrial business was sold, and separately, in December, it took steps to exit from the US bar grating market which represented 20% of its 2016 revenues.

When Frank describes our 2017 guidance, the improvement in 2017 versus 2016 in this segment will be due in part to the difficult but necessary exits that, when completed in early 2017, will benefit this segment's future profitability and returns. More specifically, this segment's operating margin for 2017 is expected to approach 10%.

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Now turning to slide 8, the Renewable Energy and Conservation segment. To begin with, the full-year 2015 amounts on this slide provide the pro forma results for the 12 months ended December 31, 2015, in order to provide an apples-to-apples comparison between the annual time periods. Regarding the revenue comparison, it's a tough comp. When 2015 benefited from accelerated order rates ahead of the then-expected reduction in the federal investment tax credit, there also was a second factor which only affected 2016 revenues. That was its concerted focus on a more profitable sales mix during 2016 to help increase its operating margins.

In looking at the bottom half of this slide 8, we all celebrate their effectiveness in focusing on mix, plus their realization of cost synergies and other actions to improve margins, because those increases in operating income and margin compared to 2015 are impressive. But it's focus on a more profitable sales mix also came with a lower growth rate to its top line in 2016. In finishing 2016, we experienced a decrease in new orders, and therefore a lower backlog to start 2017, as we were likely as not as price competitive in the final half of the year, in order to achieve the impressive operating margins.

Again, I'll get a bit ahead of Frank by noting that in the 2017 guidance we're planning a balancing of the sales mix and pricing, and sharing some of its margin improvement with customers in order to lift this segment's rate of revenue growth. Nonetheless, overarching good news for this segment, and all its employees are to be congratulated. At this point, Frank will resume, specifically describing our guidance for 2017 and the underpinnings for continued financial improvement. Please turn to slide 9, "The Opportunity Entering 3rd year 2017." Frank?

Frank Heard - *Gibraltar Industries Inc - CEO*

Thank you, Ken.

Two years ago, during our Investor Day in March 2015, we presented this slide projecting the five-year path of financial improvement using the dotted and solid lines that we could deliver, based on the combination of actions resulting from each of the four pillars of our strategy. On slide 9, we've added text boxes to show our progress after two years, 2015 and 2016, and we added text boxes in 2017 representing our 2017 guidance that we'll detail later this morning, as we again expect to deliver in 2017 more money at a higher rate of return with a more efficient use of capital. Turning to slide 10, titled "Trends Continue Up," our 2017 guidance includes the achievement of these metrics in 2017, and these positive trends are direct results of tactical actions taken by all our businesses under the four-pillar strategy. So please turn to slide 11, "4 Pillars Driving Value Creation." To reground ourselves, the Company's improvement continues to be based on these four pillars, our strategic initiatives. Slide 11 lists key achievements thus far, and in succeeding slides I'll provide more color on three of them.

But I want to comment on this slide's number 2, "Portfolio Management." We've executed on several aspects considered as portfolio management, including evaluations of product lines, customers, end markets, and the allocation of leadership time, capital, and other resources to the highest potential platforms and businesses. In 2016, as Ken cited, we decided to exit three platforms. Two were in our Industrial segment, and a third was our European solar racking business which served the residential rooftop market. One effect of these proactive portfolio management decisions is their positive effect on one of our goals of realizing a higher rate of return on invested capital, which was 11.7% in 2016, comparing favorably to 8.1% in 2015 and 4% in 2014 at the beginning of our transformation. In 2017 and beyond, we'll continue to position our human and capital resources towards more attractive projects and markets. And as pointed out on slide 11, we've completed our near-term assessments and have acted on them. We have no other assessments to contemplate or act on in 2017.

So let's discuss the other three pillars, starting with "Operational Excellence" on slide 12. Operational excellence continues to be an ongoing focus, reducing complexity, simplifying our product offering through the 80/20 initiative, and adjusting our cost structure to better support our current and future partners. Our fourth-quarter and full-year adjusted operating margin of 240 and 340 basis points respectively, were the direct result of our 80/20 simplification initiatives. All of our business units are participating and fully engaged in the process. In 2015, we achieved $11 million in savings from these 80/20 initiatives. In 2016, we achieved $22 million. So in total by the end of year two, we have well exceeded our five-year target of $25 million of pretax savings.

During 2017, as we advance through the middle innings of this 80/20 initiative, we'll focus on in-lining our manufacturing processes, which is foundation for the market-rate-of-demand replenishment process and the resulting make-versus-buy decisions. These management tools are focused on manufacturing the highest volume products for our largest customers at a much higher level of capacity utilization, allowing our people

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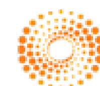

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to work effectively in a safer and more predictable environment. We expect these methods will yield additional benefits and lower manufacturing costs, reduced inventories, less fixed assets, and a higher level of service to our customer. We expect a $0.10 per share increase from the implementation of these new tools in 2017, which is an amount over and above the carryforward benefit of $0.13 benefiting 2017. And over the next 18 to 24 months as we leverage outsourcing opportunities as a result of these initiatives, our goal is to attain additional P&L savings and balance sheet improvements.

Turning to slide 13, "Product Innovation." As we detailed in slides 18 and 19, and isolating the non-recurring portions of reported revenues, our base revenues have increased and are expected to again increase in 2017 in each of our reporting segments. And within our 2017 revenue plans, there are new innovative products, the third of our four pillars. We define innovative products as those with patent protection. These currently represent 5% of our revenues, and our objective is for innovative products to approach 10% of revenues by 2020, driven initially by internal product development, but also by acquired product lines.

At our postal products business, our Xpress Locker centralized partial storage product continues to be well accepted in the market, and continues to be an exciting and expanding market in which for us to grow. In our residential roof-related products, we successfully completed the testing of a new metal roofing installation system that can withstand hurricane-force winds. The first of these roofing systems were installed in Florida, and we have received positive feedback relative to their improvements in areas of quality, building aesthetics, ease of installation, and cost in place. In our Industrial & Infrastructure segment, we focused on identifying applications outside of our traditional end markets that offer more attractive growth and margin profiles while leveraging our existing materials and manufacturing capabilities.

In 2016, we identified perimeter security as an attractive application opportunity, given the increasing demand for protecting high-value physical assets. In September, we introduced our new security fencing solution, with a growing interest by end users which is expected to contribute to this segment's top and bottom line growth in 2017. In Renewable Energy and Conservation, it's focused on continuing to expand its market share and bring to market new products targeting spaces which are adjacent to its core ground-mount racking systems. Organically, our product innovation initiatives have generated an incremental $10 million from 2014 to date, and progressed from 4% to 5% of revenues. We continue to look for ways to accelerate this progress, which is why innovation is a key part of our filter in evaluating future acquisition opportunities.

Turning to slide 14, "Acquisitions as a Strategic Accelerator" to growth. This pillar is a key part of our strategy going forward, and is our priority in use of our growing cash position. And as slide 14 displays, we have a strong balance sheet and a meaningful amount of liquidity. Our focus remains 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 our related channel partners. In October, we completed the acquisition of Nexus Corporation, a US manufacturer of commercial scale greenhouses, for further building out our Renewable Energy and Conservation segment. Our acquisition success is born from a very strict selection process that focuses on technology-rich companies with unique value propositions, combined with the potential for high returns in large high-growth markets. Our target markets for M&A continue to be the postal and parcel solutions, residential building products, perimeter security and infrastructure, water management, renewable energy and conservation. It's important that we find the right acquisitions. The key to our success in M&A to date has been our proactive prospecting and filtering versus reactive justification.

Turning to slide 15, "2017 Guidance." For 2017, we expect generally favorable market conditions aiding top-line growth for our Residential Products, Renewable Energy and Conservation segments. All three of our segments are working to expand into adjacent product categories and applications, and we expect these efforts to contribute incrementally to 2017 sales, with each segment expecting increases in its base revenues. At the same time, our consolidated results will be challenged on the top and bottom line by several factors, including difficult comparable and reported revenues, the result of exiting certain product lines, increased spending on innovative new products, and raw material price inflation. Nonetheless, taken together, we're poised to deliver a third consecutive year of sequential and meaningful financial improvement.

Now to slide 16, entitled "2017 Adjusted Earnings Growth." We've provided this reconciliation to frame the building blocks of our overall earnings improvement in 2017. Starting on the left side, we'll be challenged by a few factors, including raw material inflation, plus the continuous competitive pressures from consolidating industries, channels, and customers. Also the "Investments for Revenue Growth" representing new spending for product development and marketing to bring additional new products to market in 2017 and beyond. And, among the earnings improvement, 80/20 again will provide additional benefits in this third year, 2017.

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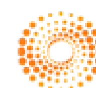

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As we also do with guidance, we provide our view of the next quarter. First-quarter 2017 revenues are expected to decrease nearly 15% compared to the prior-year period. This decrease stems from a lower order backlog as of January 1 in our Renewable Energy and Conservation segment, which was described by Ken earlier, as well as the absence of sales from portfolio management actions undertaken to exit recent product lines in order to drive higher profitability and returns. The effects of lower sales volume and rising commodity costs net of pricing actions will contribute to an expected result in GAAP EPS of between $0.10 and $0.14 per diluted share, versus $0.17 to $0.21 on an adjusted basis. After the first quarter 2017, we expect subsequent quarters to have adjusted earnings per share to be a favorable comparison to the prior-year period.

In conclusion, we remain confident in our team's ability to deliver a third consecutive year of sequential and meaningful financial improvement in terms of absolute profit dollars, returns, and cash flow. At this point, we'll open in the call up for any questions that you may have. Thank you.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Ken Zener, KeyBanc Capital Markets.

Ken Zener - *KeyBanc Capital Markets - Analyst*

Clearly, you've transformed the DNA of ROCK. I think all the questions today will be largely focused on solar. My first question is multi part. First, can you comment on the margin outlook versus the 15% level that I think Ken guided to when you guys had the third-quarter results?

And related to that, can you talk about the sales and margin cadence that you expect with a detailed explanation of the change, i.e. the industry dynamic you highlighted regarding the price competitiveness? Because it appears that's obviously impacting the 1Q outlook, A. And then why do you have confidence in the recovery for the remaining quarters?

Ken Smith - *Gibraltar Industries Inc - CFO*

Well this is Ken. I'll start on that multi-part question, Ken.

To start with, we finished very strong in the segment and for the full year 2016 it was a 17% operating margin, well above what we had imagined, but still in line where we were at the end of the first three quarters of 2016. So that high performance certainly extended through the full year.

And what we expect in our 2017 guidance for this segment is going to be in the neighborhood of 15% operating margins. So we're not anticipating a meaningful sharing of those gains as we try to accelerate the top-line growth. So it's still going to be a high performing unit inside Gibraltar, just not the outsized proportions that it had in last year. Does that help at least one part of your question?

Ken Zener - *KeyBanc Capital Markets - Analyst*

That is relative to what you're looking for for the year. And just based on the conversations I've had this morning with investors, it sounds like -- and your guidance is down 15% for sales. And your $320 guidance for the year would imply a very strong 2, 3, and 4Q growth rate relative to the first quarter. So, if you could explain how that pricing dynamic that was saving the strength in 4Q has impacted your backlog, and where that confidence comes from that once your guidance is going to be lifting up as you move into 2, 3, and 4Q?

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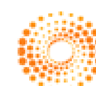

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Ken Smith - *Gibraltar Industries Inc - CFO*

Well let me put a little finer point on the 15% statistic. Only 5 percentage points of those 15 percentage points are attributable to RBI's top-line change this quarter a year ago. So the vast majority of the balance, the vast majority of the 15% is coming from product lines that we've exited, that we had reported sales in the year-ago's first quarter. So that's a strong fine point that I'd like us all to appreciate.

Ken Zener - *KeyBanc Capital Markets - Analyst*

Yes it seems -- and I'm asking this obviously respectfully, given what you guys have done, the success you've had doing things. It just seems that with the backlog slipping a bit, and if I'm not mistaken you guys had down in solar in 1Q tied to your backlog. How do you get the confidence that's going to be replenished, given that you're moving to a price component?

What happened in the market, was it the coming off the hyper competitive bids by competitors? If you could give us some more flavor there given the newness of the segment, I do appreciate this.

Frank Heard - *Gibraltar Industries Inc - CEO*

Let me give some context. I think Ken did a good job around discerning the difference in the numbers, and the materiality of some of the portfolio issues that create some tough comparables for the first quarter versus the prior year. And also, at the end of the day, you're right, the one core operating component ongoing that shows the shift in revenue is tied to the Renewable Energy piece which is the most significant acquisition we've made.

So, let me start first and foremost, the market dynamic out there hasn't changed. There's still a market that's going to grow today and long term based on our original research that we continue to validate that is going to have a 9% to 10% CAGR. So, we have no reservations that if we buy into the right space and do we have a belief that renewable energy and specifically solar is going to continue to play an ever-increasing role, regardless of policy and shifts in tax credits. So that's our opening on this.

So now it's a question of how are we affected in -- from quarter to quarter -- activity relative to the market dynamics as it relates to policies, procedures, and the related tax credits. So as we commented in the last quarter, we expected underperformance in this segment relative to its prior-year comparable 2015 where there was a forecasted end of the ITC tax credit, and there was a material drag forward of business into that fourth quarter 2015, that we expected would create a very defined and a material disadvantage from a comparable on a year-over-year basis.

That didn't materialize to the extent that we expected, and as a result we got closer. We had a better fourth quarter in 2016 than we expected, and that was primarily driven by an overperformance in our RBI Renewable Energy segment.

What also happened though was half of that, approximately, lagged of restarting of projects. It created a window of a lag that stretched from half the materiality in the fourth quarter of 2016 to drift into the first quarter of 2017. So I would say that's a very material aspect of the downturn and short term in terms of our backlog.

The pricing reference is during the same period in 2016, when we used to -- we bought a private business that used to have a philosophy of pretty much competing and wanting to win on just about every job in their ground mount space. And we thought, in addition to all the cost improvements in terms of the investments, the rolling out of new systems, the resourcing of raw material in a more cost-effective way as well as freight management, that we wanted to refocus the core talent in our organization through projects that we really thought leveraged our higher-value value proposition.

So, we've tempered the top line a little bit so that we didn't stretch out into less predictable aspects of our value proposition in terms of its delivery. So what we're doing now, if you look -- and I'm going to turn it back to Ken because he's going to talk about backlog and what we see in a real quantifiable way coming out of the fourth quarter into the first month January, and then subsequently the balance of the quarter and going forward.

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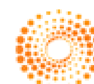

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And to be quite honest, it's a very short-term issue for us. And it's less about pricing and it's more about making sure that we're focused on the right projects going forward. And we're going to release the teams a little bit to take on more volume, now that we've got the capacity additions in house in terms of the additional roll forming equipment that we didn't have for the first two-thirds of the operating year and the back end of the year.

Despite the margin enhancement, we were really just running in some of those new roll formers and in two of the three cases in new facilities with new staff. So there is a method to the madness, so to speak, in making sure that we're aligned in terms of our resources. If we were going to take that new and incremental revenue opportunity, we didn't want to do it in an inefficient way that stretched our people and our equipment.

Today, I think we're coming through that. So that's the order of events. So, at the end of the day, and then Ken will speak to the rising backlog numbers that we have, we feel very confident that we're going to get back to at least the 9% to 10% CAGR that the industry provides us. Recognizing that in ground mount which is one of the four end markets we've gone from zero share, to 22% share, to touching into 30% share with opportunities to expand into the adjacencies as well. So no lack of confidence on our part that we're in the right space with the right company and the right team of people. Ken?

Ken Smith - *Gibraltar Industries Inc - CFO*

And to supplement Frank's points, Ken, our orders through the month -- the quarter-to-date orders thus far here in the first quarter of 2017, RBI has already booked more orders and dollar value through half of a quarter than they did in all of the fourth quarter.

And the expectation is, what they've got planned for quotes out and securing wins on projects for the balance of the quarter, they feel very confident that they're going to be back to a normalized order intake. So we've over performed and will over perform the shortfall that we had in the orders here in the fourth quarter, and that's why we continue to believe it's going to be just a short-term one-quarter effect.

Ken Zener - *KeyBanc Capital Markets - Analyst*

I do appreciate this, gentleman. And if I could perhaps put one bogey out there and see how you guys respond to it, just based on the investor questions I'm getting online right now. Is it fair to say that -- would you feel comfortable giving your guidance that's holding 2Q expectations for solar for that 10% total growth, and a mid- or low-teen EBIT margin? Is that the bogey that you guys are suggesting is fair to expect? Thank you very much, that's my final question.

Frank Heard - *Gibraltar Industries Inc - CEO*

Thank, you, Ken.

Ken Smith - *Gibraltar Industries Inc - CFO*

Well we're anticipating for the full year 2017 that this segment is going to have a 15% operating margin. And each of these next three quarters Q's 2, 3 and 4 would be favorable comparisons to its prior-year quarter as a result. Because this is not only a return to normalized order intakes, but we've also got improvements coming from their continuing programs on their cost structure and the effects of new product launches that will be coming forth after the first quarter.

Ken Zener - *KeyBanc Capital Markets - Analyst*

Thank you very much.

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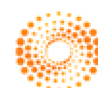

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Operator

Al Kaschalk, Wedbush Securities.

Al Kaschalk - *Wedbush Securities - Analyst*

To some extent, I may follow the prior question, but I'm wondering if there's a way to -- if you've done this and I missed it in the presentation, my apologies. But is there a way to take the $1 billion of revenue in 2016, reset that down to what you have portfolio optimized or 80/20 or exited, so that we can see that there is a, whether it's 3% growth or 2% growth? What's the growth in the components of a flat revenue -- a reported flat revenue line, that you're now guiding to for 2017?

Ken Smith - *Gibraltar Industries Inc - CFO*

Let me draw -- if everybody who has got access to the presentation slides, I'm going to talk about slide 19 in answering your question, Al, which is where we've parsed out in at least in 2016 elements of the business that we've exited. And as Frank said, we don't have any such anticipated actions for 2017.

So, if we looked at just the shaded bars in 2016 called "Ongoing Base Revenues," compared to the 2017 expectations for each of the three segments and the Company in total, I think would numerically answer your question. Where we've got 4% growth we're anticipating in Residential, 5% in Industrial and 8% in Renewables, for an aggregate consolidated performance expected this year in 2017 of the 6% increase. Hopefully, this slide can help answer that question you just posted.

Al Kaschalk - *Wedbush Securities - Analyst*

Great. And on the Renewable side, that -- the only acquisition rollover benefit is applicable to the Renewable Energy segment, and that's included in that 8% growth?

Ken Smith - *Gibraltar Industries Inc - CFO*

It is, but you can see the top of 2016, the 2016 chart, we've tried to normalize in arriving at base revenues, so that 8% rise is really their base revenues, RBI only, excluding Nexus. So Nexus is going to be incremental, but we're looking -- RBI itself has got an 8% rise coming.

Al Kaschalk - *Wedbush Securities - Analyst*

Okay. And then from a margin perspective, is the -- I think you provided the top -- the consolidated margin performance of 100 basis points improvement. Is there any particular segment that's going to be driving maybe an outsized margin contribution to the 100 basis points?

Ken Smith - *Gibraltar Industries Inc - CFO*

I'm just scanning one of my aides here. We're going to continue to - actually, the short answer is, there will be margin expansion out of our Residential segment that we are expecting. We're going to be, and now it's already at a healthy level, so its rate of expansion won't be as significant, but is still going to be climbing higher than 2016.

Industrial & Infrastructure, I'm pleased to say that we're expecting a margin expansion there. The rate is going to be substantial because we're exiting lines that we've announced that had -- they were drags in 2016. So their rate of improvement is the greatest in 2017 over last year but as it climbs to 10%.

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And in Renewable Energy, I need to correct an answer that I gave to Ken Zener, but I'll do so with answering you, Al. We finished up with our [Renewable] segment at 17% for 2016, and we're planning 2017 to be at a 15% annual margin. So after we get past the first quarter, we'll still have margin comps against 2016 that will be not as strong but we're hoping to put more money on the top line and more absolute operating income on its bottom line.

Al Kaschalk - *Wedbush Securities - Analyst*

Okay, all right. And then maybe in a broader context, that was very helpful, Ken, appreciate that. I think it will provide a little more clarity for investors as well.

In terms of the broader context, can we talk about maybe two areas or where I'd like maybe your discussions currently are: and that is, one, raw material cost. Just a reminder for some of us as to how we should be thinking about your exposure, and then your ability to pass those through if there is a timing lag.

And then secondly, given all the work you've done around the Industrial & Infrastructure space. Are you seeing signs, I won't say green shoots it's probably a poor word, but growth or project orders, things that are going to be converting to support maybe the top line growth that you're seeing and now calling for in that sector?

Ken Smith - *Gibraltar Industries Inc - CFO*

Okay. Two distinct questions, but I'll talk to the raw material factor, and I'm going to reference slide 16 where we bridged out 2016 adjusted EPS to 2017. And the second block in from the left, which is where we've put in our estimate of what we think the initial first half, primarily coming out of the first half of 2017, where -- we buy a lot of steel. It's probably 80% of our raw material purchases.

The balance being stainless, and in some resins that fill out the remaining 100% of our raw material purchases. And in the tail end of 2016 and beginning of 2017, there have been increases in the cost to buy steel. And depending on the rate of improvement and the degree of the cost, inflation triggers what pricing actions we'll engage our customers with strategically, because we certainly try to provide value, a valued product at a competitive price to our competitors.

But we've anticipated that we're going to have a $0.12 unfavorable effect here in 2017, as we work our way through what we anticipate to be some cost inflation, net of pricing actions that we anticipate that we'll be able to effect. So that's one answer to your first question.

On the Industrial & Infrastructure business, I would say we're not banking on a lot of market improvement coming out of the remaining markets that it serves. We do have some expansion in product, new product launches. Frank touched on one that we launched at the end of the third quarter of perimeter fencing, it utilizes our existing and long-standing expertise in fabricating expanded metal into a variety of end applications.

You've seen architectural facades product applications that this particular segment has taken from zero annual revenues to close to $15 million in annual revenues now. We hope to do the same here, launching and getting a full-year 2017 effect with this new product line of perimeter security fencing, which has some patented components that aid and speed the installation of such. Which has been a very attractive feature for contractors that we've sold to and bid on.

So part of this base revenue improvement in the Infrastructure & Industrial business is coming from new product penetrations. And less so from general market conditions, which I think are still going to be lackluster in 2017 across general manufacturing, process manufacturing markets that this segment serves.

Al Kaschalk - *Wedbush Securities - Analyst*

All right that's helpful thanks. I'll get back in queue.

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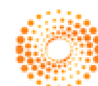

Operator

Daniel Moore, CJS Securities.

Daniel Moore - *CJS Securities - Analyst*

Maybe switch gears a little bit, Frank and Ken. Cash generation, obviously exceptional this year over $3.50 a share. How much opportunity is left in terms, with the current remaining portfolio, in terms of working capital? And do you expect working capital to be a benefit or maybe a modest headwind in 2017?

Ken Smith - *Gibraltar Industries Inc - CFO*

I'll start by ringing the bell on what our businesses have already done. So as you know, there are step changes in working capital. It's not one of these P&L sustaining year-after-year sustainment themes of cash generation sources.

And in inventory specifically, if I dialed back I think it's -- if I dialed back 21 months, just as we were getting underway in March of 2015 with our 80/20. And if I adjust our inventories and took our acquisition's inventories of Nexus and RBI's inventories at the date of acquisition, and we added it to Gibraltar's inventories then and compare it to Gibraltar's inventories including Nexus and RBI at the end of December 31, 2016, our inventories are down $50 million. On a starting base of $140 million.

I've been in accounting for a long time with manufacturers. That's an astounding drop and source of cash in such a short period of time, but it talks to the power of 80/20 simplification.

So it's a long-winded part answer to your question. That from inventory, I think there's likely more to go, particularly as we in line and only manufacture internally our highest-volume products. And turn those faster and faster through higher utilization throughout the course of a manufacturing day, a week, month, and year, and we outsource the product SKUs and inventory holdings for our smaller volume products that would be produced and held by our third parties.

So I think there's more to go in inventory, but I think the lion's share of inventory, that $50 million -- it's gone from $140 million pro forma 21 months ago down to $90 million. I don't think there's another $50 million coming out of inventory in the next 24 months, but I do think there is additional working capital improvement I think that we'll get out of the combined receivables payables action that will be beneficial and could further improve a source of cash, again step downs in the next couple years.

And besides that, I think we're also going to get some meaningful reductions in our fixed-asset base, which will, again, be one timers but it's outside the working capital element of sources of cash. So a long-winded answer, there's more to come but it may not be -- it certainly isn't the same degree of what inventories generated for us.

Frank Heard - *Gibraltar Industries Inc - CEO*

And, Dan, if you step back even further and look at the in the same context the working capital, the invested capital that we're working on prior to the two acquisitions. If I recall, the numbers in 2014 were somewhere in, total invested capital was mid $600 millions, $640 million. At the end of the day today, I think we finished somewhere in the $530 million range, $530 million-$540 million, so were down $100 million in terms of invested capital, which includes the acquisitions being rolled in there.

So in addition to the inventory component of it, the fixed assets and all the other aspects of an acquisition whether it's intangibles and so on and so forth. So very impressive progress in terms of making more money and using less from an invested capital to ultimately drive the kind of returns we're getting.

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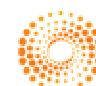

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So is there more? Yes, absolutely. To Ken's point, in inventory there probably isn't another $50 million, but certainly as we structurally change some of our footprints to focus on manufacturing the A items for our largest customers, and to some degree outsource some of the B items.

All that is going to lower our inventory levels, both at raw material and the elimination of work in process, which by and large still exists, because we still to some degree make in batch-based processes by and large. And then there is going to be a reduction in finished goods inventories on the highest new products without compromising service. Simply because the ongoing flow through of those dedicated lines will ensure that we can react in a more timely way to the marketplace, instead of pre-building three months-worth of inventory in order to guarantee a level of service.

So the corresponding part of that is that as we focus on only making A items, we're probably not going to need the same degree of fixed assets. So yes, I think if we dropped $50 million in inventory, which had originally the equal weight to fixed assets on our balance sheet, we probably only dropped just over $10 million in fixed assets. So I would expect -- you put those two together, we're not going to total $50 million, but I would be disappointed over 2017 into 2018 that we wouldn't get half the distance again.

And that is more difficult work, it's structural work. You've got to move equipment, you've got to train people in different methodologies. We've got to physically connect machines, create some automation aspects to it that maybe didn't exist in the past, and then reeducate a supply line and a series of people to ensure that we've got the raw material in the right place at the right time. So we're not done yet, but half the opportunity maybe, at over twice the period of time to get there.

Daniel Moore - *CJS Securities - Analyst*

Helpful, appreciate it. And then switching gears, in terms of new product opportunities. You mentioned metal roofing, perimeter security. Is it possible to throw out a range of market opportunity for each of those? And do you see the possibility of these areas that you would likely acquire as well, or do you see it slowly growing organically through internal R&D?

Frank Heard - *Gibraltar Industries Inc - CEO*

Well I'll just frame it, and then maybe Ken can provide some details. Certainly, the new product development areas that we're investing in is the byproduct of end-market research where we think that the markets we're targeting those new products organically to help enter are large enough and there are rising tides in terms of the types of trends that are going on in the marketplace.

And that's certainly the basis for the organic new product development is the byproduct of that end-market research. But it is also, to your point, from a strategic accelerated perspective, if we see opportunities to get there quicker than just through organic initiatives then those are the companies we're going to buy. Ken?

Ken Smith - *Gibraltar Industries Inc - CFO*

And tactically, on the aggregate of these new products that Frank noted, baked into these, that's slide 19, and our incremental base revenues in 2017 increasing, it's approximately, I think it's close to $20 million. It's about $20 million across the sum of all those new products having an impact on our top line in 2017. So it can certainly be a meaningful improvement from across the security perimeters, the adjacencies that were planning on for Residential and the solar segments as well.

Daniel Moore - *CJS Securities - Analyst*

And that's, nitpick, would that $20 million include the Xpress Locker et cetera or just the newer stuff?

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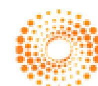
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Ken Smith - *Gibraltar Industries Inc - CFO*

It does include an element of the Xpress Lockers, yes, which is off to a really good start.

Daniel Moore - *CJS Securities - Analyst*

Got it. Appreciate it. Thank you for the color.

Ken Smith - *Gibraltar Industries Inc - CFO*

You're welcome.

Operator

Walter Liptak, Seaport Global.

Walter Liptak - *Seaport Global Securities - Analyst*

Congratulations on a great 2016.

Frank Heard - *Gibraltar Industries Inc - CEO*

Thanks, Walt.

Walter Liptak - *Seaport Global Securities - Analyst*

I'll ask some questions that expand the conversation a little bit, and but just on a follow on first. On the cash flow, slide 20, did you include any cash inflow from those fixed assets that you mentioned? And especially from the divestitures, is there any cash that we should expect in the first quarter?

Ken Smith - *Gibraltar Industries Inc - CFO*

Let me quickly, Walt, this is Ken. Let me quickly get to slide 20, because I believe what we depict on slide 20 is cash flow from operations, and that's one of four or five categories on the cash flow statement as you understand.

In a different category of the cash flow statements, we would report cash from sales of assets. So, for example, we put a press release out a week or so ago about our bar grating product line and selling that to a third party with an improvement in the cash positions to exit that. That would not be reported on slide 20.

Walter Liptak - *Seaport Global Securities - Analyst*

Oh great. How much do you think you'll be taking in net of taxes?

Ken Smith - *Gibraltar Industries Inc - CFO*

That's an approximate $10 million.

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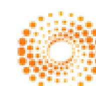

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Walter Liptak - *Seaport Global Securities - Analyst*

Okay great. And then was that the fixed assets that you referring to, or are there other fixed assets that you'd be thinking about?

Ken Smith - *Gibraltar Industries Inc - CFO*

No that's the primary source. The bar grating set of assets here in the US is of significance. It's 20% of that segment's revenue, so the asset base that goes with it is meaningful, compared to the small German solar business that we exited. So the lion's share of $10 million is really coming from the proceeds that we are advantaged by a successful sale of the bar grating assets.

Walter Liptak - *Seaport Global Securities - Analyst*

Okay, great. And then switching gears to bridge bearings. That I think is close to 10% of total Company revenues now. What are you thinking about that for growth in 2017?

And I think in your commentary, you said that 80/20 is now being implemented across the board. Is it at D.S Brown now, and are they getting benefits from it?

Frank Heard - *Gibraltar Industries Inc - CEO*

Yes. Walt, this is Frank. Let me just frame a couple things in our bridge and elevated highway business, the D.S Brown business.

It's an important segment for us, and we're not unlike others. We've always been waiting for the manifestation of the Fast Act bill that would give some confidence to the individual states and the related DOT's within them to invest in longer-term projects and more structurally meaningful projects than what was going on with just one-year extensions. And certainly D.S Brown revenue base and skill sets relate to the larger more complicated projects of bridges and elevated highways.

So in that downturn of short-term extensions, we went through a series of downsizings and operational initiatives through the 80/20 process to ensure that we aligned our cost base and our ability to serve our customers proportionately. So we get a Fast Act bill that comes out and everybody has high expectations that within a 6 month to a 12 month period of time, that money was going to quickly flow into those larger, more complicated structural projects. And ultimately that would start to show up in elevated bidding activities and release projects, and ultimately 12 months down the road because there longer cycle projects, we'd start to see that in the following year.

A year ago, we would've expected all that to start to flow in a meaningful way in terms of top-line revenue in 2017. And I think across the board and it's not unique to us, the inability of the states to match the federal dollars within the fast act I think has created some problems in terms of the expectations. Because a lot of these states have other priorities relative to balancing their budgets and providing services to their individual residents.

So I think in effect, it's been the implementation and the value of that money has been pushed out a year. We're certainly starting to see an elevated bid activity. We're certainly starting to win more of those bids.

And we expect at the back end of this year to start to see some meaningful revenue opportunities flow out of that. But I think in the end, through our planning process and what our people know, it appears that the materiality of it is really going to start to show up in 2018.

Walter Liptak - *Seaport Global Securities - Analyst*

Okay. So this year, 2017 flat revenue. Is that fair?

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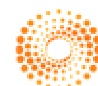

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Frank Heard - *Gibraltar Industries Inc - CEO*

With a pleasant surprise that may or may not occur, depending on some of the business in the back end of the year over and above our current planning.

Walter Liptak - *Seaport Global Securities - Analyst*

Okay.

Frank Heard - *Gibraltar Industries Inc - CEO*

Ken, do you want to add any color to that?

Walter Liptak - *Seaport Global Securities - Analyst*

No, that's -- go ahead, Ken, if you have got something.

Ken Smith - *Gibraltar Industries Inc - CFO*

No, I thought Frank gave the right answer. I didn't have anything additional to add.

Walter Liptak - *Seaport Global Securities - Analyst*

Okay great, thanks. And then, Ken, I wonder if we could just get a data point about now that the bar grating business is gone, how much O&G exposure is left, if any?

Ken Smith - *Gibraltar Industries Inc - CFO*

Well I haven't retallied it, but it's going to be quite small. For that segment, let's say they've got $200 million of revenue on our $1 billion of consolidated revenue. I don't know maybe, it's I'm going to guess it's $10 million at the most.

Walter Liptak - *Seaport Global Securities - Analyst*

Okay, great. And then last, just turning to M&A, how much capital do you think now you have available for doing acquisitions?

Ken Smith - *Gibraltar Industries Inc - CFO*

Well I think it's a lot. It's a big number, it's an ample number. In one of Frank's slides that I'm having a tough time with my lousy fingers here to find, but one of the slides we had this morning talked about accelerating our strategic growth opportunities, slide 14.

So on 14 we penciled out our current cash balance, plus our availability on current credit facilities, and what we think they could be at the end of 2017 if we didn't have any M&A activity. So it's essentially a $500 million amount of money with existing facilities.

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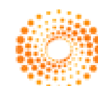

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So it's a lot to go after, hopefully meaningfully sized, more meaningfully sized prospects this year that we can successfully close. And I think we had the balance sheet and EBITDA performance, platform and runway, that if we needed additional resources we could get into those without over leveraging the Company. So hopefully 14, the numbers on it, slide 14, helped frame an answer for you, Walter.

Walter Liptak - *Seaport Global Securities - Analyst*

Oh great, yes thanks. We don't have the slides open, but thanks for giving us that number.

Ken Smith - *Gibraltar Industries Inc - CFO*

About $500 million, of which $200 million is cash.

Walter Liptak - *Seaport Global Securities - Analyst*

Okay, great. And then, Frank, how close do you think you are to getting something done in any size? And then the last question I would have just on share repurchase. I guess we've been waiting a little bit for another acquisition, could we see a share repurchase in lieu or in combination with an acquisition?

Frank Heard - *Gibraltar Industries Inc - CEO*

I'll take the first question. One of the things -- we've certainly continued to prospect in all the markets we identified, and we track about 70 different companies. And on a given day, that gets narrowed down into the 20, 25 range, and then we're constantly reviewing a short list of 4 or 5 and we're always in some form of discussions with the hope that one is going to get through the filter for all the right reasons.

In addition to that process, and that's where we stand today. In addition to that process, Ken and I, just by the nature of the improvements in our balance sheet from when we started a couple years ago, which to some degree was limiting, but even within those limits we were able to execute on RBI which has turned out very nicely for us in a variety of ways.

We're now in a position to look at companies instead of $25 million of EBITDA and below as part of our filter, we're now in a position to be able to look $50 million into towards $100 million. We've never really set our sights on those types of targets in the past, either with ourselves or working with third-party banking organizations as partners. And over the last couple months, we've certainly started that process and that has opened up a whole other series of candidates for us that would be more material in size.

Not to suggest that we just want to do one big deal, but we're not -- we wouldn't be hesitant to do it. Doing a couple deals that total up to those numbers would also be -- and being able to check a couple boxes in one or two or three of the target end markets would also fall in line. So it's our expectation and our desire to be able to work through some meaningful prospect in the first half of the year, so that we can start working on the onboarding process throughout the balance of the year and ultimately get a full-year benefit in 2018. We're confident we can do that, and that's where we spend most of our time.

Ken Smith - *Gibraltar Industries Inc - CFO*

And on your question, Walter, about share repurchase. It just so happens that in our most recent Board meeting, which happened to be 24 hours ago, at which we gave an updated view of our book financial plan for 2017, in the context of our LRP report out to them in the fall. This very topic came up around using our liquidity, continuing to fund the growth particularly with meaningful M&A to, as Frank described, and using a substantial portion of that liquidity on the right strategic acquisition and further solidify the markets that the Company participates in.

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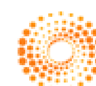

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That said, with that being our first priority for capital allocation, it's going to be a continuing question by our Directors of the Company led by Frank's recommendations on how do we use our resources. And particularly, what would be the timing and what would be the form of other uses of capital back to shareholders, including share repurchases or other means.

So it is a very recent conversation again by the Board, and its among their top-of-mind items as we continue to -- as they continue to monitor our performance and engage with Frank and the Leadership Team on how the Company is performing and filling out its ambitions on this five-year transformation. So no decisions yet, I guess is the punchline of my second answer here for share purchases. But it is top of mind.

Frank Heard - *Gibraltar Industries Inc - CEO*

Just to close that topic out, Walt, certainly not only is it top of mind, we're conscious about making progress on an acquisition perspective. We think that's the most meaningful and most valuable way we can use shareholder's money from a long-term sustainability perspective in terms of guaranteeing returns. That being said, there certainly... we'll be at a crossroads towards the end of 2017 if we haven't been able to accomplish that. To Ken's point, we'd certainly reflect hard on whether or not we'd want to go into 2018 without providing other opportunities for shareholders, in terms of the other alternatives he highlighted.

Walter Liptak - *Seaport Global Securities - Analyst*

Okay, great. All right, thanks, guys.

Operator

Thanks you. Ladies and gentlemen, 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 Heard - *Gibraltar Industries Inc - CEO*

Thank you, everyone, for joining us today and this concludes our call. Talk 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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