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# EDITED TRANSCRIPT

MOD - Q1 2017 Modine Manufacturing Co Earnings Call

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## CORPORATE PARTICIPANTS

**Kathy Powers** *Modine Manufacturing Company - VP, Treasurer, IR*

**Tom Burke** *Modine Manufacturing Company - President, CEO*

**Mick Lucareli** *Modine Manufacturing Company - VP Finance, CFO*

## CONFERENCE CALL PARTICIPANTS

**Mike Shlisky** *Global Hunter Securities, LLC - Analyst*

**Matthew Paige** *Gabelli & Co. - Analyst*

**Joe Vruwink** *Robert W. Baird & Company, Inc. - Analyst*

## PRESENTATION

### Operator

Good morning, ladies and gentlemen, and welcome to the Modine Manufacturing Company's first-quarter fiscal 2017 conference call. (Operator Instructions). As a reminder, this conference call is being recorded.

I would now like to turn the conference over to your host, Ms. Kathy Powers, Vice President, Treasurer, and Investor Relations.

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**Kathy Powers** - *Modine Manufacturing Company - VP, Treasurer, IR*

Thank you for joining us today for Modine's first-quarter fiscal 2017 earnings call. With me today are Modine's President and CEO, Tom Burke, and Mick Lucareli, our Vice President, Finance, and Chief Financial Officer.

We will be using slides with today's presentation. Those links are available through both the webcast link, as well as the PDF file posted on the investor relations section of our Company website, [modine.com](http://modine.com). Also, should you need to exit the call prior to its conclusion, a replay will be available through our website beginning approximately two hours after the call concludes.

On slide 2 is an outline for today's call. Tom and Mick will provide comments on our first-quarter results; an update on our Strengthen, Diversify and Grow strategic initiatives; and provide our revenue and earnings guidance for fiscal 2017. At the end of the call, there will be a question-and-answer session.

On slide 3 is our notice regarding forward-looking statements. I want to remind you that this call may contain forward-looking statements as outlined in our earnings release, as well as in our Company's filings with the Securities and Exchange Commission.

With that, it is my pleasure to turn the call over to Tom Burke.

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**Tom Burke** - *Modine Manufacturing Company - President, CEO*

Thank you, Kathy, and good morning, everyone.

On today's call, I will discuss our first-quarter results and provide an update on our Strengthen, Diversify and Grow strategic transformation, which we call SDG for short. After that, Mick will provide a more detailed review of our consolidated financial results and walk you through our revenue and earnings guidance for fiscal 2017. I will then provide closing remarks prior to opening it up for questions.



Despite a fairly challenging global economic environment, sales in the first quarter were up 1% on a constant-currency basis. Higher sales in our Europe and Asia segments were partially offset by lower sales in the Americas segment, which were negatively impacted by continued weakness in key end markets in the US and Brazil.

Enhanced by the decisions under our SDG initiative, we saw gross margin improve by 130 basis points to 17.8%, benefiting from improved plant operating performance, savings related to procurement initiatives, and favorable material costs. Similarly, our adjusted operating income was up \$17.4 million, up 23% from the prior year. Adjusted earnings per share were \$0.21 for the quarter, up \$0.07 or 50% from the prior year.

Although our topline continues to be challenged by weakness in certain of our end markets, I am pleased that our proactive initiatives are putting us in a place to succeed and that we have once again delivered year-over-year earnings improvements. We are clearly seeing the benefits of the cost reductions realized from our Strengthen initiatives, while also spending significant resources on various growth opportunities that will help us achieve our goals of our Diversify and Grow initiatives.

Now I would like to briefly review the segment results. Turning to page 6, sales for the Americas segment decreased 11% year over year on a constant-currency basis, primarily due to continued weakness in the commercial vehicle and off-highway markets, partially offset by higher sales to automotive customers.

All of our major OE customers in the heavy-duty truck and off-highway markets are feeling the impact of the extremely slow markets. Heavy-duty truck inventory levels remain relatively high in North America and our off-highway customers continue to signal minimal optimism for future volume increases.

Gross margin improved by 110 basis points from the prior year, up to 17.9%, despite the drop in sales for the quarter. Our gross margin benefited from lower material costs and savings from our ongoing procurement initiatives. Despite this margin improvement, gross profit was down \$1.6 million year over year, due to the lower sales volume.

SG&A was down \$1.1 million, or 7%, primarily due to continued cost-control efforts. The team in the Americas segment has been working hard to lower costs in light of the challenging market conditions. We have significantly lowered our operating expenses in Brazil over the past 18 months and have reduced headcount in North America as well.

Adjusted operating income for the Americas segment was down 4% to \$11.5 million, due to lower gross profit resulting from the lower sales volume in the quarter. As expected, we are planning for difficult end market conditions to continue to impact our year-over-year sales comparisons in fiscal 2017.

In North America, the heavy-duty commercial vehicle market has continued to decline from its peak volume last year. We continue to expect the overall market to be down about 25%. Also, the heavy-duty portion of the off-highway market is still declining year over year, with key customers continuing to reduce their orders.

In Brazil, the recession continues and we see no sign of near-term improvement. Although these market conditions are challenging, we remain diligent in our commercial efforts and believe that we are well positioned competitively to take advantage when these markets rebound, which we expect they will.

Please turn to page 7. Sales for our Europe segment continued to be strong and increased 9% in the first quarter on a constant-currency basis as a result of higher sales to automotive and commercial vehicle customers. Gross margins improved by 570 basis points from the prior year to 17.2%, driven by the higher sales volume, favorable materials cost, and improved operating performance.

Adjusted operating income was up \$9.1 million to \$14.7 million, due primarily to the higher gross profit on sales.



I am very pleased with the operating performance of the European region. This significant earnings improvement resulted from not only converting on the higher sales volume, but also from achieving savings targets and stabilizing production at facilities that had capacity-related production issues last year. A great deal of work has been done to improve the margins in Europe and we are clearly seeing the results.

As you know, our European business has undergone significant transformation over the last few years. None of this has been easy, but it created momentum, helping lead us to our profitability targets.

We still have work in front of us. As I previously mentioned, we are expanding capacity in Hungary and are actively quoting from our two cost-competitive Hungarian locations. This is the next step for Modine towards providing a truly global design for truck radiators, something we were unable to achieve with the Origami design. We have had technical and commercial success with our next-generation radiator design in other regions around the globe and are pleased to be able to offer it to our European customers going forward.

This is important as some of our existing commercial vehicle programs start winding down later this year, putting short-term pressure on our topline in the region. As a result, we expect the gross margin percentage to be lower than this quarter, but to continue to show improvement over the prior year.

Please turn to page 8. Sales for our Asia segment were up 35% compared to the prior year on a constant-currency basis. This improvement was primarily related to higher sales to automotive and off-highway customers in China and incremental sales related to our recently formed joint venture, Modine Puxin.

As you may recall, Puxin primarily produces stainless steel heat exchangers for the light-, medium-, and heavy-duty commercial vehicle market in China. The joint venture is off to a strong start, demonstrating its competitive position in local markets. We expect a continued contribution to the growth of this segment as we expand our product offering in China to support higher emissions standards. This is also allowing us to diversify our customer base with domestic OEs across all vehicular markets.

Operating income for Asia segment increased \$1.1 million to \$1.5 million in the first quarter, primarily due to higher sales volumes and lower SG&A expenses.

Turning to page 9, sales for our Building HVAC segment were flat on a constant-currency basis as lower product sales to the school market in North America were offset by increased sales in the UK. Gross margin for the segment decreased 260 basis points to 25.1%, primarily related to the UK business.

In the UK, gross margin was down due to operating inefficiencies, competitive pricing pressures caused by the strong pound versus the euro, and higher depreciation expense related to the replacement assets associated with the Airedale fire. We have made progress in addressing the operating inefficiencies and expect our gross margin to improve in the remaining quarters of the year, due to an improved cost base, normalized pound to euro currency rates, and regaining our capacity in the new facility.

Adjusted operating income was down \$0.8 million to \$1.3 million, primarily due to lower gross profits, partially offset by decreases in SG&A expenses.

As a result of the weaker-than-expected market conditions and the uncertainties surrounding the Brexit vote, we are lowering our outlook for Building HVAC markets for the remainder of the year. Specifically in the UK, the Brexit vote has caused uncertainty in the markets and capital investment has slowed. However, the British pound has weakened against the euro since the Brexit vote, which has eased competitive and pricing pressures in the short term within the UK market.

In response to the market uncertainty, we implemented a program of workforce reduction in the UK that included early retirements, voluntary redundancy, and compulsory redundancy actions. We expect to see savings from these actions beginning next quarter.

Please turn to page 10. Before turning it over to Mick, I would like to give an update on our Strengthen, Diversify and Grow financial objectives. As a reminder, we have two core goals related to this strategic framework.

Our first objective is to achieve gross cost reductions of \$40 million to \$50 million, designed to help us move toward a higher operating margin of 7% to 8%. The cost reduction is a cumulative target and will more than offset general economic inflation and contractual price downs to our customers.

Second, we are looking to acquire at least \$100 million of incremental non-vehicular revenue and expand our leverage ratio between 1.5 and 2.5 times. We are specifically targeting transactions that are immediately accretive to our shareholders and that will generate sufficient cash and synergies to allow us to quickly pay down debt so that our leverage remains in our targeted range.

As it relates to our first goal, we are making significant progress. To date, we have identified or implemented actions that will lead to \$36 million total gross savings on an annual run rate basis. To achieve these savings, we have focused on SG&A reductions, manufacturing footprint savings, and our global procurement initiative.

We have implemented a variety of programs aimed at headcount reduction, including the early retirement program in North America that I mentioned last quarter and the workforce reduction program in the UK. We are making progress towards our global product-based organizational structure and are focusing on additional ways to reduce SG&A spending without compromising our business.

In terms of our manufacturing footprint goals, the Washington, Iowa, transfer and associated closure continues to run ahead of schedule and will be completed by the end of this calendar year. Our savings to date include the benefits of the McHenry closure last year and a projected benefit from the Washington, Iowa, closure.

For our procurement initiative, we continue to identify and implement meaningful savings opportunities as we work through a wide range of product value streams.

Now moving to the critical Diversify and Grow objectives, while I don't have anything specific to share at this time, I can assure you that we have identified growth opportunities that will help us meet these objectives. In the past, we have talked about the internal resources we have dedicated to business development activities. We have a solid pipeline of potential acquisitions and we are very encouraged about several opportunities that may be actionable. We are investing significant resources on these objectives and we're optimistic about having something more definitive to report soon.

With that, I would like to turn it over to Mick for an overview of our consolidated financial results and to review our fiscal 2017 guidance.

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**Mick Lucareli** - *Modine Manufacturing Company - VP Finance, CFO*

Thanks, Tom, and good morning. Please turn to slide 12.

Our first-quarter sales increased slightly, despite the fact that we continued to experience weakness in certain end markets. Sales increased 1% on a constant-currency basis, excluding a small, unfavorable currency-exchange impact of \$1.6 million. Higher sales in Europe were driven by improvements in our automotive and commercial vehicle markets. Sales in our Asia segment continue to increase due to higher launch volumes of our automotive engine products. These increases were mostly offset by continued weakness in global off-highway markets and in the North American heavy-duty commercial vehicle market.

I am happy to report that our gross margin improved 130 basis points to 17.8%, despite the relatively flat sales. This improvement was driven by lower commodity prices, improved plant operating performance, and savings from our procurement initiatives. As Tom outlined, we are clearly seeing the benefits of our Strengthen, Diversify and Grow initiatives in the operating results.

Moving on to SG&A, costs were higher than the prior year by \$2 million, or 4%. The increase was due to two items. First, we incurred higher professional fees related to business development activities as we continue to pursue inorganic growth opportunities. In addition, we also had higher employee benefit and incentive compensation expenses compared to the prior year.



Also during the quarter, we recorded \$2.3 million of restructuring expenses. The majority of these charges relate to employee severance, equipment transfer, and plant consolidation costs in the Americas and Building HVAC segments. The bottom portion of the table shows these adjustments. As usual, we've included a full reconciliation between our reported results and our adjusted operating results in the appendix.

First-quarter adjusted operating income of \$17.4 million was up \$3.2 million, or 23%, from last year. This was the result of our improved gross margin, combined with ongoing cost control. Adjusted EPS was \$0.21, up \$0.07 or 50% compared to last year.

Our improvement in EPS was driven by both improved operating earnings and lower income tax expense. As I discussed in the past, our tax rate is impacted by our mix of foreign and domestic earnings. This mix resulted in lower effective tax rate this quarter.

Once again, we are pleased with the financial performance this quarter. The management team remains highly focused on the items that we can control. Despite relatively flat sales volume, we once again improved our operating earnings, providing direct evidence of this focus.

Turning to slide 13, free cash flow in the quarter was negative \$8 million. This is \$5 million better than the prior year, due to cash generated from reductions in working capital and lower capital expenditures. This was expected and is consistent with previous years as we have a large number of cash flow items in our Q1.

Our balance sheet provides plenty of liquidity to support our growth and diversification initiatives. We ended the quarter with \$107 million of net debt, up \$13.5 million from prior year-end. We also ended the quarter with \$64 million of cash and a net leverage ratio under one.

We did not repurchase any stock during the quarter. As Tom mentioned, we're working hard on growth opportunities and preserved cash to maximize flexibility, consistent with our message at the start of the share repurchase program.

Now let's turn to our fiscal 2017 full-year guidance on slide 14. We are confirming our fiscal 2017 full-year sales and earnings guidance. We expect sales to be down 1% to up 3% from the prior year. Throughout the Americas segment, we expect difficult market conditions to continue in the near term. This includes ongoing weakness in our global off-highway market and in the North American commercial vehicle market. We are taking a cautious approach to the business environment in Brazil, given the Olympics and continuing difficult economic condition.

Also, certain end markets have softened in our Building HVAC business. We will have better visibility once we get closer to the heating season. And the global automotive business remains a bright spot. This is clearly benefiting both our Europe and Asia segments in particular.

We expect adjusted operating income to be \$65 million to \$71 million. This equates to an increase of 3% to 12%. We will continue to drive margin and SG&A improvements through actions planned as part of our SDG initiative.

We expect our adjusted EPS to be between \$0.77 and \$0.87, with our full-year tax expense to run between \$16 million and \$18 million. As always, this expense is contingent upon the actual country-to-country mix of earnings.

I would like to point out that, similar to the last two years, we anticipate a seasonal slowdown in Q2. We expect the sequential change in Q2 will look very similar to last year. However, that will be followed by sequential improvements in Q3 and Q4, resulting in a stronger second half.

With that, Tom, I will turn it back to you.

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**Tom Burke** - Modine Manufacturing Company - President, CEO

Thanks, Mick.

Overall, I am pleased with our earnings improvement this quarter, despite the continued market challenges in North America and Brazil. Our European business showed significant sales and earnings growth and our Asia segment continues to benefit from automotive oil cooler launches in China and new business opportunities for our new joint venture.



We are focused on driving operational improvements in the UK and will continue to work towards our savings goals and the various initiatives under our Strengthen, Diversify and Grow program. On top of this, we continue to devote a considerable amount of time and energy to achieving our growth and diversification objectives.

I will close by recognizing that Modine recently celebrated an important milestone, our 100th anniversary. Relatively few companies can achieve this longevity and I'm honored that Modine is among them. It has been very rewarding for our management team to attend employee celebrations around the world, and I am very proud to be a part of an organization that has been in business for over a century. We are all committed to setting this Company up for the next century in business. We want to thank you for your continued interest in Modine.

And with that, we will take your questions.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions). Mike Shlisky, Seaport Global.

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**Mike Shlisky** - *Global Hunter Securities, LLC - Analyst*

Nice quarter.

Maybe I will start with the news of the day here, the Class 8 orders for the month of July. I want to get your thoughts, since you are the first company out there that is speaking in a public forum this morning. Pretty weak in July, as you probably heard; it has been weak for most of the year.

I guess, can you maybe tell us perhaps since your last call in June, I see you didn't really change your overall outlook, but since the last call in June, do you feel like your major OEM customers in North America have gotten any more cautious about their build days or their outlook here?

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**Tom Burke** - *Modine Manufacturing Company - President, CEO*

No, our outlook is just as I described it at this point, although we just saw that data come in this morning as well, overnight from the report. So, clearly, that was a very weak July. So we are looking cautiously at our releases and will be in close contact with our customers going forward as to see any adjustments that they may be doing as far as production changes. But as of this point, nothing to report that we have seen since our last report, Mike.

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**Mike Shlisky** - *Global Hunter Securities, LLC - Analyst*

Okay. Great. Perhaps now that we're going to be entering some companies' summer shutdown periods, is there any kind of run-through perhaps in some of your bigger markets, perhaps auto in Europe, trucks in North America, trucks in Europe, et cetera? Do you think companies have increased their amounts of shutdowns this summer versus last summer? Just some thoughts about what you think companies are doing to either other bunch more production onto certain days or just work through lower volume orders this year.

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**Tom Burke** - *Modine Manufacturing Company - President, CEO*

I can't really give you a general answer to that question. Clearly, we are looking at all customers' releases and right now, as I said earlier, we anticipate probably adjustments lower, but as far as a pattern of what we are seeing, they're planning for shutdowns going forward. We can't see a general



pattern, although we are anticipating changes based on the July numbers, as you mentioned. So I imagine we will see some downward pressure and some changes in releases going forward, but nothing I can report on in general. Mick, anything you are picking up?

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**Mick Lucareli** - *Modine Manufacturing Company - VP Finance, CFO*

No, nothing to add.

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**Mike Shlisky** - *Global Hunter Securities, LLC - Analyst*

Okay. I also want to ask about your material cost benefits that you saw in the fiscal first quarter here. Can you maybe clarify or bucket it, what portion of it was from -- directly from the SDG program and what was just you are picking up a good price versus your cost and your sales price in the market? I am wondering what was controlled by you and what is going to stick going forward and what might fluctuate going forward of that savings?

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**Mick Lucareli** - *Modine Manufacturing Company - VP Finance, CFO*

Mike, in the quarter we had about \$4 million of just LME-based benefits, and I would say about half of that is also due to the transaction premium, the Midwest transaction premium. So I would say about \$2 million in the quarter is due to, call it, pass-through that we will eventually pass through to the business segments, and then from a pure procurement savings side, we had \$3 million to \$4 million of savings in the quarter.

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**Mike Shlisky** - *Global Hunter Securities, LLC - Analyst*

So that was incremental on top of the market price from --

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**Mick Lucareli** - *Modine Manufacturing Company - VP Finance, CFO*

[Right].

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**Mike Shlisky** - *Global Hunter Securities, LLC - Analyst*

Okay, got you. And those kinds of savings in procurement you think are here to stay, for the most part, correct?

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**Mick Lucareli** - *Modine Manufacturing Company - VP Finance, CFO*

Correct.

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**Mike Shlisky** - *Global Hunter Securities, LLC - Analyst*

And, also, was there any benefit in the quarter from taking content out of the product? In other words, making things lighter or use less materials as well in the quarter? That you know of?

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**Mick Lucareli** - *Modine Manufacturing Company - VP Finance, CFO*

Nothing from a design standpoint.





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**Tom Burke** - *Modine Manufacturing Company - President, CEO*

No.

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**Mike Shlisky** - *Global Hunter Securities, LLC - Analyst*

All right, guys. I appreciate the answers. I will hop back in the queue. Thank you.

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**Operator**

Matthew Paige, Gabelli & Co.

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**Matthew Paige** - *Gabelli & Co. - Analyst*

I was wondering if you could provide any color regarding your data center business.

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**Tom Burke** - *Modine Manufacturing Company - President, CEO*

Our data center business is based out of the UK, in Leeds, specifically, and so we have a combination of what we called precision air conditioning, data center room, and the matching chiller production that goes along with that.

Sales out of that business is about \$70 million annually and really supports, more or less, the UK and some exports to mainland Europe and also the Middle East. That's the general overview of that.

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**Matthew Paige** - *Gabelli & Co. - Analyst*

Right, right, but do you have any color on data center performance in your first quarter?

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**Tom Burke** - *Modine Manufacturing Company - President, CEO*

Yes, clearly sales were down on the data center market. As we've identified, there has been some weakness and more uncertainty in the UK markets with capital investment being lower, and we anticipate because of slowing in construction potentially in the UK with the Brexit vote that we are dropping our guidance in that to essentially flat performance going forward versus an increase in sales before.

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**Matthew Paige** - *Gabelli & Co. - Analyst*

Perfect. I appreciate the color and thanks for your time.

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**Operator**

David Leiker, Baird.



**Joe Vruwink** - Robert W. Baird & Company, Inc. - Analyst

This is Joe Vruwink for David. This has to be one of the strongest above-market growth quarters for Modine in some time. I am wondering, do you have a sense of either a dollar value or a percentage growth rate for what new business might have contributed to your results? Because it seems, obviously, end markets are weak. To put up a positive organic print is a pretty good result.

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**Tom Burke** - Modine Manufacturing Company - President, CEO

In general, as we mentioned in Asia, all the growth is from new business wins, okay, on the oil cooler launches in the automotive segment, some commercial vehicle business as well, but mostly automotive in the Asia region. And, again, new business wins in Europe are also promoting it.

As far as specific magnitude, Mick, do you have any feel for that?

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**Mick Lucareli** - Modine Manufacturing Company - VP Finance, CFO

Yes, maybe just anecdotally, Joe. I would agree and it is really the strength, as we commented on the automotive side. You know the challenges on off-highway and clearly the recent on the Class 8, but when you look at -- we look at our growth in automotive across the world.

In the Americas, we were north of 15%, 20% type automotive growth in the quarter. In Europe, excluding the BMW we were up high single digits with the BMW wind-down. Excluding that BMW, we were 10% to 20% type sales growth in Europe. And then, obviously, in Asia with the 30% growth rate in revenue, that was almost all automotive based. So clearly across the world, our automotive business is outstripping -- or outpacing the market growth.

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**Joe Vruwink** - Robert W. Baird & Company, Inc. - Analyst

So just sticking on the automotive business for a second, and after all the work that has been done, Modine might end up being an automotive, primary automotive supplier again by the end of this cycle. But there is clearly some disruption going on in the competitive landscape where you are filling a niche in market, and I think one market you haven't participated in as much historically would be on the Japanese thermal side. And I think the Japanese automakers have been showing more than openness to maybe moving away from the traditional suppliers.

Is that an opportunity ultimately for Modine or do you think there's enough growth just staying within your supplying, supplying some of your current core customers, thinking primarily the German automakers?

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**Tom Burke** - Modine Manufacturing Company - President, CEO

Clearly, premium German producers in Europe have really been a big catalyst for us, specifically as it relates to automotive growth in Asia.

However, saying that, we do have opportunities to expand our traditional markets and nothing to report on today, but clearly we are looking at, I would say, other Asian-based OE producers, including Japanese. I might also include Chinese domestic suppliers as well.

So, all in all, I am very pleased with what we call our product-focused approach towards attacking our markets. And we're leveraging those building blocks and using them very well, and it is really paying off from the standpoint of what I would say building a scalable advantaged position in the market in these areas such as oil coolers, liquid charge-air coolers, and other related devices that really directly mount to the engine.

In addition, we are also being very diligent in our approach to our powertrain cooling products. Again, we have transitioned away from what I would say a traditional Tier 1 in the past in the module and really focused on component strategies that can support that market specifically not only through traditional internal combustion engines, but, as you know also, in electric vehicle where you have some powertrain-related type components that are needed in that market.

So I just think we are being, what I would say, very smart with our approach and our product strategies and looking where we can grow that into adjacent markets, including a new customer market that we haven't been participating as much in the past.

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**Joe Vruwink** - *Robert W. Baird & Company, Inc. - Analyst*

And then, two follow-ups on your Asia business specifically, if I may. The first would be it looks like an \$8 million, so year over year, increment if I strip out currency. Is \$8 million a quarter a good run rate for new business contribution in Asia this year?

And then, my second question would be on the end market, China truck market specifically, you have had some companies not participate in the strength. It seems like it is dominated by certain OEMs that might be a little aggressive on pricing. It seems like Modine is seeing some benefits from the market. So maybe just an update on your customer exposure within the Asia region.

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**Tom Burke** - *Modine Manufacturing Company - President, CEO*

So, Mick, you want to go first?

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**Mick Lucareli** - *Modine Manufacturing Company - VP Finance, CFO*

Yes, just on the math, we have got in the quarter, it is about \$7 million, excluding currency impact, is the topline growth. And I think the organic piece, I think \$6 million to \$7 million a quarter is sustainable as we look at what is built into our full-year outlook, Joe. Tom?

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**Tom Burke** - *Modine Manufacturing Company - President, CEO*

As far as Asia commercial truck customers, I have to take it a little bit country by country. In India, which we have got a very well-established business and we have got significant powertrain cooling business with both global and domestic truck producers in India, we found that we compete very well in the open market with what we call and you heard me say that we have a new next-generation global truck radiator that we are really moving on from the Origami technology and really established its capability first in India.

We have extended that to China, where we have landed a domestic OE truck producer of significance in China and are working through our new joint venture, which has been Puxin, now Modine Puxin, has been established in the commercial vehicle business for a significant amount of time. It brings great relationships that we are looking at expanding with some of the leading, if not the leading, truck producer in China as well, with an opportunity from the relationship side.

So we feel very positive with what we are doing specifically and also very comfortable with our, let's say, margin performance that we can deliver there.

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**Joe Vruwink** - *Robert W. Baird & Company, Inc. - Analyst*

Great. I will leave it there. Thank you.

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**Operator**

Mike Shlisky, Seaport Global.



**Mike Shlisky** - *Global Hunter Securities, LLC - Analyst*

Take my follow-up here. I wanted to ask about the diversification and grow parts of the strategy here. I know you can't give us anything specific, but can you maybe tell us what might come first? Is it possible that you might see some kind of M&A announcement before we see some kind of diversification through organic growth and your own designs into new product lines? Tom, give a sense on a timeline as to where we might be expecting to see some of these other things fall into place.

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**Tom Burke** - *Modine Manufacturing Company - President, CEO*

Timeline-wise, clearly we wouldn't be talking as much that there weren't really actionable items that we are engaged in. You also heard Mick say that we are investing a amount of resources and expenses to make sure that we are doing this properly.

So, first, I want you and the rest of our shareholders to rest assured that we are being very disciplined in this process. So we have walked away from more than we have considered actionable because of not meeting our objectives of being out of the chute accretive.

Number two, hitting a nice strategic fit with our base business in the industrial segment, being building HVAC or the coils business. So, that's the approach timeline.

I guess it is really dependent on when the egg is ready to hatch, but we are clearly far down that process to be able to say that we are optimistic that we can bring together something soon, okay, and that's about as far as I can go on that. Mick, anything to add to that?

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**Mick Lucareli** - *Modine Manufacturing Company - VP Finance, CFO*

The one thing I would add, I think from a materiality standpoint, a move the needle standpoint, our expectation would be that an announcement of an acquisition or some sort of business growth in that manner would be the first to come.

We have made organically, Mike, we have made significant investments in air handling and the HVAC space and ventilation products and geothermal products. But off a base of \$250 million, \$300 million versus the \$1.23 billion of vehicular, it is hard organically to move the needle in a rapid way.

So, I agree with everything Tom said, and then as far as something materially changing, the next step would be if we were able to execute on one of these opportunities.

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**Tom Burke** - *Modine Manufacturing Company - President, CEO*

Then, Mike, I would like to add, and I'm glad Mick brought that up, this is by no means saying we're deemphasizing anything in the vehicular business. As a matter fact, the Modine Puxin joint-venture recent announcement demonstrates that we're going to continue to assure that we have a very strong and capable product portfolio able to deliver globally to our targeted markets in a very disciplined manner. So I just want to make sure that's on top of that.

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**Mike Shlisky** - *Global Hunter Securities, LLC - Analyst*

Okay, got you. I appreciate the color. Thank you.

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**Operator**

I am showing no further questions at this time. I would now like to turn the conference back to Kathy Powers.

**Kathy Powers** - *Modine Manufacturing Company - VP, Treasurer, IR*

Thank you. This concludes today's call. Thank you for joining us this morning and thank you for your interest in Modine.

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