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MOD - Q2 2016 Modine Manufacturing Co Earnings Call

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PRESENTATION

Operator

Good day, ladies and gentlemen. And welcome to Modine Manufacturing Company's Second Quarter Fiscal 2016 Conference Call. At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session and instructions will follow at that time. (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.

Kathleen Powers - ***Modine Manufacturing Company - VP, Treasurer & Investor Relations***

Thank you. Thank you for joining us today for Modine's Second Quarter Fiscal 2016 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 for today's presentation. Those links are available through both the webcast link as well as a PDF file posted on the Investor Relations section of our company website modine.com. Also, should you need to exit the call prior to its conclusion a replay is available through our website beginning approximately two hours after the call concludes.

On slide two is an outline for today's call. Tom and Mick will provide comments on our second quarter results and provide an update to our revenue and earnings guidance for fiscal 2016. At the end of the call, there will be a question-and-answer session.

On slide three is our notice regarding forward-looking statements. I want to remind you that this call may contain forward-looking statements as outlined in today's 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.

Thomas Burke - ***Modine Manufacturing Company - President and CEO***

Thank you, Kathy and good morning, everyone. On today's call I will first discuss two important announcements the company made last night, then we'll cover our second quarter results. After that Mick will provide a more detailed review of our financial results. I will then provide final remarks prior to opening up the call for questions.

Last night, we announced our new Strengthen, Diversify and Grow strategic platform for the future. We outlined this plan on Page 5 of our supplemental slides. This is an important transformative step for Modine that will enable us to evolve into a more diversified thermal management company while being aggressive in our efforts to increase long-term shareholder value. We have created a plan to guide our actions. This plan has three major components.

First, we will strengthen our business by implementing a global product-based organization. We believe this new organization will improve our speed to market and allow us to capture synergies among our vehicular, Building HVAC and coils businesses. We will also leverage our global scale to optimize our manufacturing footprint and drive cost reductions throughout our business. This also includes a comprehensive overhaul of our procurement process that we expect to significantly reduce our total spend on materials and services. Finally, we will optimize our vehicular product portfolio to drive higher operating margins and leverage technology drivers in building blocks within our product portfolio.

Second, we will diversify our business. We will invest significant financial and human resources in our industrial businesses, which today includes Building HVAC and Coils. This will create a more balanced exposure to our end markets, decrease our customer concentration and reduce cyclicality. Increasing the resources allocated to Building HVAC and Coils will bring more focus to higher margin, organic and inorganic growth opportunities, while allowing us to build global market-leading positions in Building HVAC and Coils. Through more concentrated resource allocation in these areas, we expect to achieve more appropriate market recognition and value for these two important businesses.

Third, we will grow our business. This means aggressively pursuing strategic acquisitions, primarily in the Building HVAC and Coils markets. We are looking at both large and bolt-on targets. We clearly have the balance sheet capacity to grow through acquisition but will be responsible with the amount of leverage we carry.

In addition, we will focus our R&D, product development and commercial pursuits in high-growth vehicular areas. We have favorable industry trends that will continue to require innovative thermal management solutions. We will leverage our advantaged global designs and our building block product strategy to increase our market share.

This is an ambitious plan. Our customer and competitor dynamics are changing rapidly and we must adjust our business to position Modine for a long term market leadership position. By strengthening, diversifying and growing our business we will improve our margins, while lowering our dependence on cyclical markets. The successful execution of our plan will result in significant growth and earnings improvement.

Refer to Page 6 in our supplemental slides for a snapshot of the plan’s targets. To strength our business, we will increase our operating margin from a current state of 4% to 5%, to 7% to 8% by the end of fiscal 2018. This will be accomplished through expansion of our current low-cost manufacturing footprint, SG&A reductions and savings achieved through our global procurement project. Overall, we are targeting $40 million to $50 million of annual savings from these initiatives over the next 18 months.

Our Diversify goals are to reduce our customer concentration and cyclical exposure by increasing our Industrial business as a percentage of our portfolio from the current state of 15% to 20%, to 30% to 40% or roughly double in size.

I want to be very clear about something though. This does not mean we are de-emphasizing our core vehicular business. As is clear from our stated goals, this will remain a critical part of Modine. In order to grow our business, we plan to target at least $100 million of incremental industrial revenue through acquisition by the end of fiscal 2018. We will approach any acquisitions in a disciplined manner and we recognize that our ability to achieve this goal depends on a number of factors, some of which are outside our control.

We are also targeting a net debt-to-EBITDA ratio of between 1.5 and 2 times. We feel this is a responsible amount of leverage for our business. However, we acknowledge that we may operate outside this range at times due to economic changes and in order to pursue compelling acquisition opportunities. The Company will pursue acquisitions that make sound business sense, are aligned with our strategic priorities and that are accretive to the business such that they will allow us to return to our target leverage ratio of 1.5 to 2.5 times within a reasonable period.

Please turn to Page 7. In addition to the announcement about our strategy, we also announced that our Board of Directors authorized a repurchase of up to $50 million of shares, which will expire on November 3, 2016. We'll make our decisions to repurchase shares or suspend the buyback program based on a number of factors including ongoing assessments of the capital needs of the business, stock price, and general market conditions. Although our priority remains to invest in our business, we believe we can reach our targets while providing a return to our shareholders.

Now, I would like to move on to discuss our second quarter results starting on Slide 8. Sales in the second quarter were down 2% on a constant currency basis with decreases in the Americas segment more than offsetting increases in all other segments. Adjusted operating income of $8.1 million was down $800,000 from the prior year and adjusted earnings per share of $0.04, were $0.01 lower than the prior year. Adjusted operating income was negatively impacted by $1.2 million of foreign currency. Excluding these impacts, both adjusted operating income and adjusted earnings per share would have increased year-over-year. With the first half of the fiscal year completed, we expect our second half earnings to be significantly stronger than the first half.

Mick will go through the consolidated results in greater detail but now I will review the segment performance for the second quarter.

Turning to Page 9. Sales for the Americas segment decreased 11% on a constant currency basis with lower sales in both North America and Brazil. Brazil is mired in a recession that has continued to deepen and we don't believe that we have found the bottom yet. Sales in Brazil were down 18% on a constant currency basis with decreases to both vehicular OE and aftermarket customers. Aftermarket sales normally increase in a recession as consumers repair, not replace, their vehicles. However, this is not occurring in Brazil which demonstrates the severity of the economic downturn. In response, we have transitioned to a four-day work week and expect to stay on this schedule for at least six months. We've reduced our workforce in Brazil by one-third and continue to identify synergies between our North and South American businesses. We expect to see the savings from these cost reduction efforts in the second half of the year. In North America, sales were down 10% with lower sales to off-highway and commercial vehicle customers. Our off-highway sales were down due to continued weakness in the agricultural equipment and mining sectors and our commercial vehicle sales continue to be impacted by changes in our customer's market shares.

Gross margin improved by 190 basis points from the prior year to 16.3% as the impact from lower sales volume was more than offset by improved operating performance, lower material costs and savings from the closure of the McHenry facility. Adjusted operating income for the Americas segment was up $300,000 to $8.7 million despite the significant drop in sales and a $300,000 negative currency impact. This is excellent performance from this segment considering the significant market and currency challenges.

In the second half of the year, we expect to see higher earnings in the Americas segment. We have significant launch activity that will benefit the topline and we are continuing to win business throughout the segment. We have additional savings from the McHenry closure and cost savings initiatives in Brazil. We have lowered our break-even point in Brazil and will continue to make adjustments as needed. Finally, we expect to have year-over-year savings from lower material costs. All of this will lead to a stronger second half of the year. All-in-all I am very pleased with how our Americas teams have responded to the adverse market conditions in this segment.

Turning to Page 10. Sales for our Europe segment increased 4% in the second quarter on a constant currency basis, as higher sales to automotive and commercial vehicle customers were partially offset by lower sales to off-highway customers. The European automotive and commercial vehicle markets remain strong and we expect moderate growth to continue for the rest of our fiscal year.

Gross margin improved by 10 basis points from the prior year. The positive impacts from higher volumes and favorable material costs were partially offset by volume-related manufacturing inefficiencies, due to high automotive volumes. As I mentioned last quarter, we are working at full capacity, I mean 24x7 capacity at certain production facilities in Western Europe, which has driven up costs for shift premiums and expedited freight. In response, we're adding furnace capacity at our plant in the Netherlands and transferring production of certain product lines from these high-volume plants to our Hungarian facilities, where we will also be expanding capacity. In particular, we are in the process of acquiring the land adjacent to one of our Hungarian facilities and plan to proceed with a phased expansion of this facility. This will allow us to increase our competitive position in Europe and fully alleviate our current capacity constraints.

We also expect our Europe segment to have higher earnings in the second half of the year. Adding furnace capacity in Netherlands will stabilize our manufacturing process, reducing direct labor costs, premium freight and scrap. We also expect to benefit from lower materials costs in the second half of the year.

I'd like to take a second and address how the recent announcements by Volkswagen may impact our business. As many of you know, Volkswagen is a very significant customer for us, both in automotive and commercial vehicle markets. We have automotive products on both diesel and gasoline engines across many of their brands. However, it is important that I point out that Modine did not supply any of the components at issue in the investigation. At this point, we have not seen any volume change from VW. If they lower their orders in the future, it likely would impact our business, but we have no way to assess the likelihood of that or quantify the potential impact at this time.

Turning to Page 11. Sales for our Asia segment were up 1% compared to the prior year on a constant currency basis. Increased sales to automotive customers in China and India of $4 million were partially offset by lower sales to off-highway customers in China and Korea of $3 million. The off-highway market in China has continued to weaken with excavator production 30% lower than the prior year and approximately 70% off the market high. Market conditions are worse than expected and we don't anticipate any improvement in the second half of our fiscal year.

The automotive market is stable and we continue to benefit from increased launch volumes of automotive oil coolers. These programs will continue to ramp up in the second half of the year, offsetting the continued declines in the off-highway market. Our operating loss was higher than the prior year due to higher personnel costs we’re investing in the region.

Turning to Page 12. Our Building HVAC segment had another very good quarter. The segment sales increased 11% in the quarter on a constant currency basis. This increase was largely driven by higher sales of heating and ventilation products in North America where the market continues to be strong. In the UK, our sales were up slightly with increases in sales of air handling units offset by lower sales of data center cooling products. The stronger British pound is creating competitive pricing pressures particularly for export to mainland Europe.

Gross margin for this segment increased 70 basis points on the higher sales volumes during the quarter and operating income was up $700,000 to $3.9 million. We expect higher sales in the second half of the year for the Building HVAC business as compared to the first half, primarily due to seasonality of our heating business. We are preparing for another strong season in North America and our current order intake indicates a sequential increase in sales in the UK as well. Work continues to progress on the re-build of our manufacturing facility in UK after the fire that destroyed our building in 2013. We are still on track for construction to be completed in December with the plan to have all business functions moved out of our temporary facilities to the new building by the end of our fiscal year in March.

With that, I'd like to turn over to Mick for an overview of our consolidated financial results and guidance.

Michael Lucareli - ***Modine Manufacturing Company - VP, Finance & CFO***

Thanks, Tom and good morning, everyone. Please turn to Slide 14. Our financial results on this page have been adjusted to exclude $1 million of restructuring expenses and a non-cash charge of $39 million related to a voluntary pension lump-sum payout as described in yesterday's press release. The lump-sum payout reduces the size, the risk, volatility and cost associated with our U.S. pension plans. We succeeded in reducing our pension obligation by over $60 million. We recorded $30.9 million of the settlement loss to SG&A expenses and the remaining $8.3 million to cost of sales.

Our U.S. GAAP income statement is included in the appendix of this presentation and in our earnings release along with reconciliations. As anticipated, we experienced slightly lower volumes in our second quarter due in part to our typical summer seasonality. We also continued to experience significant market softening and foreign exchange headwinds. As a result, our second quarter sales were down 11% primarily due to the strength of the U.S. dollar compared to last year. And as Tom mentioned, sales decreased 2% on a constant currency basis, excluding an unfavorable exchange rate impact of $35 million. On a constant currency basis, sales improved in Europe, Building HVAC and Asia. However, these increases were more than offset by lower sales in the Americas segment, where we experienced continued weakness in Brazil and in the North American off-highway market.

I am pleased to report that our gross margin improved by 120 basis points to 16.2% despite the decline in sales and the inclusion of $1.3 million of consulting expenses related to our global procurement project. The improvement was driven by lower material costs and better conversion in our Americas and Building HVAC segments. With the higher margin, our gross profit was up 3% excluding $4.2 million of negative foreign exchange rate impact.

Moving on to SG&A, costs were lower than the prior year by $1.9 million and the exchange rate impact was favorable at $3.1 million in the quarter. Excluding the favorable exchange rates, SG&A was up 2.5% from the prior year. A significant portion of the increase came from higher commissions in our Building HVAC segment on higher sales volume.

Q2's adjusted operating income of $8.1 million was $800,000 lower than the prior year. This excludes the $39.2 million lump-sum pension settlement expense and the $1 million of restructuring costs. However, our adjusted operating income does include $1.3 million of procurement consulting costs, which we incurred in support of our future savings goals. And adjusted operating income was up 4.5% on a constant currency basis and 19% when excluding FX and the procurement consulting fees.

Adjusted earnings per share of $0.04 were down $0.01 from the prior year. We are pleased with the overall performance this quarter, considering the lower sales volumes. We improved our gross margin, controlled our SG&A spending and positioned ourselves for a stronger second half of the year. Last, we are starting to see the positive impact of our previous cost saving efforts and restructuring actions. This includes the headcount reductions in Brazil and the recently completed closing of our McHenry plant.

Turning to slide 15, free cash flow in the quarter was $18.5 million driven by an improvement in our operating cash flow. Working capital levels and capital expenditures were lower than the prior year. Our free cash flow in the first half of the fiscal year was $5.5 million and we continue to expect positive free cash flow for the full fiscal year. Our balance sheet remains strong and we ended the quarter with a net debt to capital ratio of 19% and $65 million of cash. Our Board recently authorized a $50 million share repurchase plan, which gives us the ability to repurchase shares on an opportunistic basis. While we see solid value in our stock price, especially in light of our new strategic direction, we plan to balance the repurchase efforts with our priorities of investment that support diversification and growth. And we believe that we are in a strong position with a solid balance sheet to make these significant investments in the company and provide a return to our shareholders.

Now let's turn to our full year guidance on Slide16. While we are being proactive with our cost controls and thinking long-term with strategic actions we announced, we do continue to face challenges in many of our key end markets. As most of you know, more than 60% of Modine sales are located outside of the United States, with a heavy dependence in both Europe and Brazil. We estimate the full-year exchange rate impact will likely be $110 million on the top-line. Also, approximately 15% of our sales are tied to the very challenged global agriculture, heavy construction and mining markets. Similar to last year, we expect a stronger second half based on several factors.

First, our topline should benefit from new program launches in our Americas and Asia segments. This is driven by several automotive programs with customers such as Tesla and General Motors. Also, we are approaching the heating season in our Building HVAC segment, which typically provide higher sales and profitability.

Last, but not least, we expect to benefit from our restructuring actions in Brazil and North America and also expect to achieve higher operating efficiencies in several of our European plants. We are trying to manage these projected benefits with the concerns of further volume declines in Brazil or China. The team is also focused on balancing the procurement costs and savings during the balance of the year. With this in mind, we have provided the following guidance for fiscal 2016: Sales down 2% to 7% from the prior year, which is slightly lower than our previous guidance of flat to down 5%. However our constant currency sales guidance is actually flat to up 5%. Please note that at this time we are trending towards the lower end of our sales guidance range, also we have not included any impact from the public announcements of VW as we haven't seen any information that would cause us to lower our forecast. Adjusted operating income is anticipated to be $65 million to $70 million and is unchanged from our previous guidance.

This range equates the earnings growth of flat to up 7%. On a constant currency basis, we expect the adjusted operating income to be up 6% to 13%. Our adjusted earnings per share guidance of $0.75 to $0.82 or up 19% to 30% is also unchanged. We have a lot of hard work in front of us in order to combat the market challenges and achieve our financial goals. However, many of the improvements in cost reductions that we've been working on and that we announced yesterday are within our control. Additionally, we announced a solid strategic framework that will allow us to strengthen, diversify and grow our business, so that we will be less exposed to the cyclicality of our end markets and better positioned to grow and add value for shareholders. I look forward to reporting on our progress next quarter. Tom?

Thomas Burke - ***Modine Manufacturing Company - President and CEO***

Thanks, Mick. This is an exciting time for Modine. We're working hard to transform our business and I am pleased that we're able to do so from a position of strength. Our business will be more diversified and we will be able to provide higher returns to our shareholders throughout the market cycle.

Moving to a global product-based organization is a right thing to do. It will provide us with several advantages. We will increase our speed to market and leverage our global scale, while we continue to optimize our manufacturing footprint and take costs out of the business.

We have a strong balance sheet and we'll use that capacity to grow and diversify our business by investing in the segments with the highest growth and margin profiles, primarily the building HVAC and coils businesses. As I mentioned, our objective is to increase our non-vehicular revenues from 15% to 30% to 40% of our business within the next three years. At the same time, while we are looking for these investments, we have the ability to provide a return to our shareholders by opportunistically repurchasing Modine's stock. The successful execution of our plans will clearly result in a transformation of our business, one that leads to significant earnings improvement and a more diversified global business. With that, we will take your questions.

QUESTION AND ANSWER

Operator

(Operator Instructions) David Leiker, R. W. Baird.

David Leiker - ***R. W. Baird - Analyst***

Good morning, everyone.

Thomas Burke - ***Modine Manufacturing Company - President and CEO***

Hi, David.

David Leiker – ***R. W. Baird - Analyst***

So, in terms of the steps, the actions that you've announced here today, I'm sure it's more complicated than this, but we've essentially taken the three vehicles, regional segments, collapsing them in the one and then you're building products, is that the right way to look at this?

Thomas Burke - ***Modine Manufacturing Company - President and CEO***

Yes, the right way to look at this David is and I'm kind of go back to our last organizational change in 2006 and 2007, where we went from a divisional structure to a regional structure supported by global product lines running through each regional segment. It was a great step forward and brought a lot of strengths to the Company. What we're doing now is taking that and actually concentrating our product lines as a businesses' P&L divided into certain product groups globally.

So, we will kind of take the regional structure P&L and transform it towards a product line P&L globally ran so we could optimize the product strategy, the synergies across each of the segments and to prioritize which products and allocate accordingly. So, it's going to be a real true global product line. Again, it's going to be hitting all regions but we're just removing the P&L and the decision rights of product strategy and focus in leveraging in a smart way to a full global product line.

David Leiker – ***R. W. Baird - Analyst***

Now, despite you having a regional structure, I do believe did introduce product development across the regions. When you talk about optimizing that portfolio, if you know the baseball analogy, where would you be in that because you've already taken quite a few actions in that regard.

Thomas Burke - ***Modine Manufacturing Company - President and CEO***

Yes. I mean I guess baseball analogy inning, is that what you are talking about, what inning are we in, as far as....

David Leiker – ***R. W. Baird - Analyst***

Yeah.

Thomas Burke - ***Modine Manufacturing Company - President and CEO***

Yes, so.

David Leiker – ***R. W. Baird - Analyst***

In terms of optimizing the product portfolio.

Thomas Burke - ***Modine Manufacturing Company - President and CEO***

Yes, so I mean, we have strong global product strategies include our powertrain cooling, engine, now we're developing our coils and of course Building HVAC. And I would say that we're probably into the late innings of work that can do. This is the last step, I guess we're bringing in the key reliever right now. Okay, if you would use that analogy to close it out, okay and get us to make those decisions. I don't want to say we've suboptimized our product strategies, but we don't fully gain the opportunity by saying we're going to capitalize once, we're going to leverage this capacity, we're going to engineer it once, we're going to go through that portfolio of 52 product lines and optimize the best way to get the contribution out of each of those. That's the way to look at it.

David Leiker – ***R.W. Baird - Analyst***

Yeah. I guess, something that came across my thoughts along the way as you're talking is this isn't necessarily a step function change how much you're doing, it's a next step of the evolution of the path that you've been on for the last eight or nine years. And this is the last step that kind of optimized that structure, as you've been all through that journey, is that the right way to look at that?

Thomas Burke - *Modine Manufacturing Company - President and CEO*

You actually said it better than I did. Okay. This is actually the next, the last natural evolution of how to get to where we need to go to, yes.

Michael Lucareli - *Modine Manufacturing Company - VP, Finance & CFO*

David, it's Mick, Just to add to that, when we did our last reorganization a number of years ago, went to the global product base structure, there were a number of products and businesses we exited and we've continued that discipline of looking at the lower return, lower margin products. So, just to emphasize what Tom said and from my seat, this is really about optimizing our global product platforms and in some regions we are very well, we're very strong and have the product platform and how you take that to other regions of the globe or leverage it, which is very different than big pieces of the company going to have to be carved up or sold off. We've gone through that heavy lifting already.

David Leiker - *R.W. Baird - Analyst*

Yes. I guess, from my point this is an incremental change, not a radical change, I guess is the --.

Thomas Burke - *Modine Manufacturing Company - President and CEO*

Very good point.

David Leiker – *R.W. Baird - Analyst*

And then, just two last items here. If you look at the opportunity increased market share, there has been a lot of consolidation in the thermal space, do you have the scale and the product capability to compete in that environment as you got much larger competitors today than you had a few years ago?

Thomas Burke - *Modine Manufacturing Company - President and CEO*

We definitely feel we do and it varies by product family. Okay, obviously in certain areas like our engine products group, we are a leading market share participant in global range that we're supporting all the major global automotive suppliers with unique engine products and we expect to expand that. On powertrain cooling, a little bit more challenging in certain products, especially when you get to automotive, but on commercial truck and off-highway, we feel very strong, especially vehicle we feel very strong about. So each one varies in degree and this change, this next step of evolution is going to allow us to really concentrate on honing on those strengths we have, allocate the capital resources appropriately and make sure we gain, the opportunity is there for us to take and also maybe deemphasize, I only use that word at any one market but certain products are just don't hit that return on capital and we don't see in the future, but we can make sure we can take that resource and capital and put that to work in a different place.

David Leiker – *R.W. Baird - Analyst*

Again, then the last item here is on the margin target, the 78% by fiscal 2018. If I recall correctly, you've always had a target similar to that. Some might look at this as, you need to take these actions to get to that number or you could come out that this was always part of the process of getting to that level of profitability with or how should we look at that?

Michael Lucareli - *Modine Manufacturing Company - VP, Finance & CFO*

I'll take the question first and then Tom can add. The way we've approached and looked at it, David is yes, we've had this target out there for a while. If you recall, when we originally did our four point plan, the biggest difference here is, there have been a lot of ups and downs in the market. And as we look forward with everything, we know what's going on and the off-highway market, heavy equipment; volume has been the biggest challenge including FX. If we had all of the market tailwinds behind us and all of the heavy lifting we've done to get our footprint right, we can clearly get to our operating margin goals, but in addition given the climate we are in, we want to accelerate that and not strictly depend on volumes. So what we are doing here in addition to all the strategic benefits Tom laid out about being leaner, faster, more consistent globally, these actions are really going to move us more rapidly towards our goals regardless of what happens to the topline and in the end-markets.

David Leiker – *R. W. Baird - Analyst*

Okay. Great. Thank you very much.

Thomas Burke - *Modine Manufacturing Company - President and CEO*

Thank you.

Operator

(Operator Instructions) Mike Shlisky, Seaport Global Securities.

Mike Shlisky - *Seaport Global Securities - Analyst*

Can you hear me.

Thomas Burke - *Modine Manufacturing Company - President and CEO*

Hi Mike.

Mike Shlisky - *Seaport Global Securities - Analyst*

Okay. Great. Just a few quick questions on the new strategy here. In the past, you've discussed entering a lot of non-truck and auto markets, such as the white goods market, the commercial vehicles, et cetera, are there any other new areas, that you're going to be targeting as a part your plan to diversify here, outside of those two or three new categories you've been talking about recently?

Thomas Burke - *Modine Manufacturing Company - President and CEO*

No, I think what we really tried to specifically say that our very well established Building HVAC presence both here and in the UK and our coils business is well established and now growing to $60 million in the near future, in North America has leading North America position, both of those are areas that we are going to leverage for our non-vehicular expansion and growth. We have adjacent opportunities that go from there, so you can go into the pure industrial areas that we are looking to expand as opportunities that could include things like, power generation and things along those nature, plus the coils market opens up an opportunity to get into other areas it could be food processing and other things of that nature. So we feel there is a lot of expansion opportunities that we have in our ability to grow because of the strong established positions that are non-vehicular related and they're growing at sizable rates already. Okay. So, we want to build on that with both organic and inorganic opportunities.

Mike Shlisky - *Seaport Global Securities - Analyst*

And then within vehicular going forward, do you plan to maybe change the mix between truck and auto? Is it -- I would assume it's little bit better probably in truck right now as far as margins are concerned. Is that a piece of it and if so with certain truck markets entering somewhat of a down phase here, which could last for a couple of years and how you plan to address getting those volumes, good enough to kind of keep the margin going?

Thomas Burke - *Modine Manufacturing Company - President and CEO*

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Well, I think the best way to say is, that we've always been a strong truck market supplier and we always continue to be a strong truck market supplier, making sure that we optimize our business there. On the automotive side, clearly the technical trends going on with fuel efficiency and that type of thing, really offer a lot of opportunity for us to look at both electrical vehicle, which we are doing well, as we've talked with Tesla and a growing opportunity with the Model X, but other electrical suppliers as well, but also inside of that we -- let's say traditional internal combustion engine opportunities as they need more fuel efficiency, we have lots about air and engine content that we're looking at. So we look at, again I stressed it in my opening comments that we are in the vehicular business, where we're strong in the vehicular business in all the segments including auto and truck and off-highway are going to be still core to our future. So I guess that's the best way for me to answer that.

Mike Shlisky - ***Seaport Global Securities - Analyst***

Okay. I'm going to just throw in two more here. The first one being on procurement. How challenging is that going to be (inaudible) started it sounds like, but how challenging would that be to kind of get to where you want to go there, given that you've got such low commodity prices today currently. Is it a matter of changing how you imagine your actual scale of your orders, your freight costs, your kind of locking in prices over time or if we see the prices of let's say copper or aluminum go up from here, is that a challenge to getting those kind of upside, is that a challenge to kind of fulfilling this kind of plan basically?

Thomas Burke - ***Modine Manufacturing Company - President and CEO***

Yeah. I want to kick start and I'd like Mick to finish up on the details of which you are talking about. We've been working on this for a while. Okay. And as Mick alluded we spent $1.3 million investigating, developing and really globalizing our procurement processes. This is another great example with our strategy going forward as we are really going to globalize these key functions, support functions that integrate with the business in a strong manner. So we feel very confident with the targets, to answer your question. We have not been optimizing our $700 million to $800 million purchase spend, we kind of done that more regionally than is ideal and by globalizing these buys whether it be on raw material or purchase components or services and (inaudible) we see and then have proven and have compared ourselves, we really have the opportunities to build on this. Mick, you want to add to that?

Michael Lucareli - ***Modine Manufacturing Company - VP, Finance & CFO***

Just as in what I would add Mike is that through our analysis, we've backed out the raw material content and obviously we can't control raw material prices in that, but the controllable portion of our spend is where we really see the value and it is for the reason that Tom said, becoming a truly global organization with more global standards is going to allow us to consolidate our supply base and consolidate the complexity of the number of parts we buy and the number of people we deal with in a major way. So it is a huge opportunity for the company as we go forward. And we're still really excited about it.

Thomas Burke - ***Modine Manufacturing Company - President and CEO***

Let me build on little. These actions that we're talking about today weren't built in the last few weeks. We've been working for months and for months and even to the beginning of year working with our Board and developing how we can get ourselves to this kind of position going forward. So each one of these elements that we've defined, have been thought through and gone through benchmark against our competition on how get to market and the speed at which we need to move and I just want to make sure that, Mike, that you understand, this is something that has a lot of deep thought review and analysis and process development to get to this point.

Mike Shlisky - ***Seaport Global Securities - Analyst***

Got it, yes, sure, perfect. And then just kind of throwing one last one here on the other side, outside of the program here. I was little surprised on your Building HVAC outlook here. I mean it's certainly very positive but I mean, I am seeing construction trends up double digits and if you exclude oil and gas which isn't in building, we are up over probably about 15% in certain parts of the country. So, is there any upside here you think possibly to Building HVAC or is perhaps some of this due to we have to kind of wait and see how cold it gets until we change the outlook here?

Thomas Burke - ***Modine Manufacturing Company - President and CEO***

Well, cold weather definitely helps the heating business, there is no doubt about that. There is a direct correlation but we have the leading market share position on heating in North America. We have a developing growth strategy in ventilation business both in what we call the school business and also commercially with our Atherion product line growing in North America and so the trends there will continue on a positive way is the modernize and replace, we are getting a big installed base, is another big driver for sales for us. On the data center process, our UK business in Leeds has the leading position in the UK, expanding that into the Middle East, where there are growth opportunities. Again, the drivers of that with the digitalization, we see favorable growth. And the ventilation acquisition we made in Barkell is going to complement that a lot because there is a trend of moving to what we call more free cooling we've talked about in earlier calls, to really build up lower energy cost to build that computer digitalization capacity has been driven by the Internet of things. So we feel we see growing strong growth trends that are going to continue in those markets where we're specifically placed.

Mike Shlisky - *Seaport Global Securities - Analyst*

Okay, great. I'll leave it there. Thanks guys.

Operator

And I'm showing no further questions at this time. I would now like to turn the conference back to Kathy Powers for any closing remarks.

Kathleen Powers - *Modine Manufacturing Company - VP, Treasurer & Investor Relations*

Thank you, this concludes today's call. Thanks for joining us this morning and thank you for your interest in Modine. Good bye.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This concludes today's program. You may all disconnect. Have a great day.