05-Nov-2019

Myers Industries, Inc. (MYE)

Q3 2019 Earnings Call

CORPORATE PARTICIPANTS

Monica Vinay
Vice President, Investor Relations & Treasurer, Myers Industries, Inc.

Andrean R. Horton
Interim President & Chief Executive Officer, Myers Industries, Inc.

Kevin L. Brackman
Chief Financial Officer & Executive Vice President, Myers Industries, Inc.

Mike Valentino
Group President-Distribution, Myers Industries, Inc.

OTHER PARTICIPANTS

Tyler J. Langton
Analyst, JPMorgan Securities LLC

Christopher Sinnott
Analyst, Cowen & Co. LLC

MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by and welcome to the Myers Industries' Q3 2019 Earnings Conference Call. At this time, all participants are in a listen-only mode. After the speaker's presentation, there will be a question-and-answer session. [Operator Instructions] Please be advised that today's conference is being recorded. [Operator Instructions]

I will now like to turn the conference over to your speaker today, Monica Vinay. Please go ahead.

Monica Vinay
Vice President, Investor Relations & Treasurer, Myers Industries, Inc.

Good morning. Welcome to Myers Industries' third quarter 2019 earnings call. I'm Monica Vinay, Vice President of Investor Relations and Treasurer at Myers Industries. Joining me today are Andrean Horton, Interim President and Chief Executive Officer; and Kevin Brackman, Executive Vice President and Chief Financial Officer. Also joining us on the call today and available to answer questions are Mike Valentino, Group President, Material Handling Segment and Chris DuPaul, Group President, Distribution Segment.

Earlier this morning, we issued a news release outlining the financial results for the third quarter of 2019. If you've not yet received a copy of the release, you can access it on our website at www.myersindustries.com under the Investor Relations tab. This call is also being webcast on our website and will be archived there along with the transcript of the call shortly after this event.

Before I turn the call over to Andrean and Kevin, I would like to remind you that we may make some forward-looking statements during the course of this call. These comments are made pursuant to the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995. Such statements are based on management's current expectations and involve risks, uncertainties and other factors which may cause results to differ materially from those expressed or implied in these statements. Further information concerning these risks, uncertainties and other factors is set forth in the company's periodic SEC filing and may be found in the company's 10-K filing.

I am now pleased to turn the call over to Andrean Horton.

Andrean R. Horton

Interim President & Chief Executive Officer, Myers Industries, Inc.

Thanks, Monica. Good morning, everyone and thank you for joining us. I'm pleased to be speaking with you today as the company's Interim President and CEO. Before we review the results for the third quarter and our outlook, let me say a few words about the CEO transition. I first want to thank Dave Banyard, on behalf of the board of directors for his leadership of Myers over the past four years. Dave was instrumental in my joining Myers and his dedication to the company and our people will have a lasting impact. The Myers board of directors has commenced the search process to identify a permanent CEO to lead the company. In the interim, I appreciate the board's confidence in me and I'm excited to work closely with our senior leadership team.

I want to emphasize a few key points that should give investors' confidence. First and foremost, it is my responsibility as Interim CEO to ensure that our strategic, operational and financial priorities are clearly understood and executed especially during this time of transition. And I can assure you that our entire executive leadership team is committed to executing on these priorities. Despite the current market headwinds, we remain focused on serving our end market, controlling our costs, executing our key initiatives and we are ready to capitalize on opportunities that may arise along the way. In short, your company is in capable hands.

With that introduction, let's get to the review of our third quarter results. Generally speaking, we continue to see softness in several of our key end markets, particularly in the Material Handling Segment. Despite these demand headwinds, we were pleased to generate a solid 10% increase in Distribution Segment revenue and our overall focus on price cost optimization across the portfolio boosted gross profit margins and we drove nearly 8% increase in year-over-year adjusted operating income.

If you turn to slide 3 of the presentation, we'll share an overview of the accomplishments and challenges we saw in the third quarter. Let's begin with a high level review of our achievements. In August, we completed the acquisition of Tuffy Manufacturing. Tuffy aligns well with our overall growth strategy and extends Myers Tire Supply's leadership position in the commercial fleet market. As you'll see in our results, the acquisition contributed nicely to the growth we saw in our Distribution Segment during the quarter.

In addition to integrating Tuffy during the quarter, our Distribution Segment also continued to execute on its transformation plan. Excluding the impact of Tuffy, sales increased for the fourth consecutive quarter and adjusted EBITDA margin increased 190 basis points to 9.5%. We continue to be on track to meeting our Distribution Segment EBITDA margin goal of 10% by the end of 2020.

On a consolidated basis, adjusted operating income increased by almost 8% despite a decline in net sales of 7% during the quarter. The organization continues to drive continuous improvement processes and cost discipline throughout our operations and we are pleased with the progress we've seen today. We generated $22 million of free cash flow during the quarter which puts our year-to-date cash flow as a percent of sales in line with the prior year and closer to our target of greater than 9%.

Now let's review some of the challenges we had during the quarter. In our Material Handling Segment, we recorded a charge of $3.5 million for estimated product replacement costs related to a manufacturing defect identified during the current quarter in an isolated number of legacy boxes. Once the issue was identified, we immediately performed root cause analysis and implemented corrective action. Additionally, we have worked closely with the impacted customer through collaboration and transparency to ensure a high level of satisfaction is achieved and the issue is fully remediated.

Moving on key end markets in Material Handling continue to experience several challenges during the quarter. In our food and beverage end market, sales declined year-over-year primarily as a result of lower the seed box sales. We believe this is due in part to the late planting season in the farm sector and limited CapEx spending following some customer consolidations within the market. Kevin will address this later along with trends for the upcoming ag season.

In our industrial end market, sales were down due to softer than anticipated orders from a few of our larger customers for some of our military packaging products. Because the business is project based it's difficult to accurately forecast when demand for those products will pick up. At this point, we aren't expecting to recover that volume in the fourth quarter. Although we did realize incremental fuel can sales volume in our consumer end market during the quarter as a result of Hurricane Dorian, it was not enough to offset the soft demand that continued from the first half of the year as a result of the unprecedented wet weather during the start of the lawn and garden season.

Finally, sales to RV customers continue to decline which was not unexpected. As we've mentioned before, during the softer demand period in the RV market, we are taking steps to consolidate our manufacturing operations. We estimate that this consolidation process will be completed in 2020 with an expected annual savings run rate of $1.5 million beginning next year.

Our focus on gaining market share with our current customers and pursuing new customers has resulted in some wins over the last few quarters. Overall, the quarter reflected the continued success of the Distribution Segments transformation and the margin benefits of our focus on price cost optimization.

Now I will turn it over to Kevin to go through a financial review of the quarter.

Kevin L. Brackman

Chief Financial Officer & Executive Vice President, Myers Industries, Inc.

Thanks, Andrean, and good morning everyone. Today I'll review our 2019 third quarter financial performance including our balance sheet and cash flow. Please turn to slide 4 of the presentation and I'll begin with a review of our third quarter operating performance. All numbers in the presentation reflect continuing operations. Net sales for the third quarter were $125 million, a decrease of 7% compared to the third quarter of 2018. The decrease was primarily due to a decline in the Material Handling Segment within the company's food and beverage and industrial end markets. Adjusted gross profit margin increased 20 basis points to 31.5%. This was primarily due to a favorable price cost margin which more than offset the lower sales volume and the charge we took during the quarter for estimated product replacement costs that Andrean discussed earlier.

Our adjusted operating income increased 8% to $8.5 million for the quarter. This was the result of the higher gross profit margin as well as a decrease in adjusted SG&A year-over-year due primarily to lower variable compensation costs and savings from the Distribution Segments' transformation initiatives. Adjusted diluted earnings per share were $0.15 or flat compared to the third quarter of 2018. GAAP earnings per share were $0.15, compared to a loss of $0.60 for the third quarter of last year. GAAP earnings per share in the third quarter of 2018 included $33 million of charges that we took related to the 2015 sales of the lawn and garden business.

Now let's turn to slide 5 for an overview of our performance by business segment. Net sales in the Material Handling Segment decreased 14% to $84 million. The decline was driven by sales decreases across all of the segments end markets. The sales decreases by end market were highlighted earlier in the presentation by Andrean and are outlined here as well.

Despite the lower sales Material Handling's adjusted EBITDA margin increased 90 basis points to 18.4% which was primarily due to favorable price cost margin and lower incentive compensation costs. In Distribution, net sales increased 10% to $41 million excluding the Tuffy acquisition which contributed $2.4 million in sales during the quarter, net sales increased 4%. Distribution's adjusted EBITDA margin increased to 190 basis points to 9.5% as a result of the higher sales volume, savings from the segment's transformation initiatives and the Tuff acquisition. The segment continues to execute its transformation plan which includes enhancements in its go-to-market strategy, the implementation of 80/20 to drive improved contribution margins and optimization of its logistics and overhead costs with a goal to expand the EBITDA margin to 10% by the end of 2020.

Turning to slide 6, we generated free cash flow $22 million in the quarter, compared to $12.7 million for the third quarter of 2018. The higher cash flow was mainly due to a decrease in working capital year-over-year which was primarily the result of lower accounts receivable due to the softer sales volume and a reduction in past due accounts. Working capital as a percent of sales at the end of the third quarter was 4.7%, which was in line with the previous quarters.

Now let's turn to slide 7 for our 2019 outlook for our end markets. As Andrean outlined earlier, several of our key end markets are challenged at the moment, and we saw the results of that in the third quarter. This trend is expected to continue into the fourth quarter. As a result, we now anticipate that sales for 2019 will be down high-single digits versus our previous estimate of down low to mid-single digits. I'll go into some detail now on the drivers behind that.

Starting at the top with our consumer end market, we continue to expect that for the full year this market will be down high-single digits. As we had anticipated, the softer market demand that we saw in the second quarter continued into the third quarter. Additionally because we launched the new fuel container late last year, we don't anticipate the same level of sales volume during the fourth quarter of this year given that the fourth quarter is traditionally a softer quarter for fuel container sales. As a result, we've forecasted sales to be down in this market during the fourth quarter.

In our food and beverage end market, we are lowering our outlook. We now anticipate that this market will be down double-digits for the full year, compared to our previous outlook of down mid-teens. As we've stated earlier, a portion of the decline came during the first quarter of this year as there was a difficult year-over-year comparison due to a very high season in early 2018. Additionally, there has been a high degree of uncertainty across the ag sector. While that uncertainly has continued into the fourth quarter, we've had indication from some of our customers that demand for the fourth quarter will be softer than previously expected. While we do anticipate continued success in the food processing portion of our business, our volumes in that market coupled with the growth we are experiencing are not yet large enough to offset the overall impact of the ag portion of this end market.

Turning to our vehicle end market, we continue to expect to be down high-single digits primarily driven by the decline in sales to RV customers that has been ongoing throughout the year. In our industrial end market, we've updated our outlook from up low-single digits to down low-single digits to reflect the sales decline we experienced during the third quarter as a result of softer than expected demand for our military packaging products. The pace of business with our industrial distributors remained steady to slightly down.

Finally, in our auto aftermarket, we've updated our outlook from up low to mid-single digits to up mid-single digits as a result of incorporating the incremental sales we anticipate from the Tuffy acquisition.

Turning the slide 8, I'd like to review our updated outlook for 2019 annual guidance. We've already discussed the updated sales outlook. So let's start with D&A and net interest expense. We've lowered our guidance for D&A and net interest expense to $24 million and $4 million respectively versus $25 million and $5 million previously. No changes were made to the anticipated effective tax rate of 27%, diluted share count of 36 million shares or capital expenditures of $10 million. We are updating our EPS guidance ranges and are now expecting GAAP EPS to be in the range of $0.65 to $0.70 versus $0.62 to $0.72 previously and adjusted EPS in the range of $0.75 to $0.80 versus $0.75 to $0.85 previously.

The updated GAAP and adjusted EPS guidance reflect the decreased sales outlook and the charges for the estimated product replacement costs partially offset by a decrease in incentive compensation costs. The updated GAAP EPS guidance also reflects the reversal of approximately $2.3 million of stock compensation costs that we expect to recognize in the fourth quarter resulting from the October departure of the company's CEO.

I will now turn the call back to Andrean for some closing comments.

Andrean R. Horton

Interim President & Chief Executive Officer, Myers Industries, Inc.

Thanks, Kevin. Before we take questions, let me close with this comment. The inherent cyclicality of some of our businesses will always be a challenge, but one we are working to address. We are beginning to see the impact of our segmentation efforts in each of the businesses as we look to drive focus in markets that we've identified as key for longer term growth. While it will take us some time to scale these market segments, our early results are having a positive impact. Additionally, the work that our teams have done and continue to do like rationalizing our manufacturing footprint and executing continuous improvement processes will also enable us to perform better than we would have through down cycles in the past. In summary, we remain focused on executing our strategy and continuing our progress in serving our end market.

With that, we will now open the line to questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from the line of Tyler Langton with JPMorgan. Please go ahead.

Tyler J. Langton
Analyst, JPMorgan Securities LLC

Q

Good morning. Thanks for taking my questions.

Monica Vinay
Vice President, Investor Relations & Treasurer, Myers Industries, Inc.

A

Good morning.

Andrean R. Horton
Interim President & Chief Executive Officer, Myers Industries, Inc.

A

Good morning.

Tyler J. Langton
Analyst, JPMorgan Securities LLC

Q

Thank you. Just had a question I guess on the seed box sales. I guess it's Q4 and Q1 are the big seasons and I know you mentioned sort of [indiscernible] (00:17:50) wondering how much visibility at this point do you have on those two quarters.

Mike Valentino
Group President-Distribution, Myers Industries, Inc.

A

Sure. Good morning Tyler. This is Mike. We're starting to get some feedback and visibility from our customers. I'd say we've got a better outlook on the softer demand that we're seeing here in the fourth quarter than we do in the first – on what's going to happen in the first. And we'll talk about the first quarter outlook and forecast in our next call at this point. But we've got some visibility and it's similar to what you've seen in the past, where you've heard from us in the past, excuse me, though on what we're and what we expect to happen in the fourth quarter here around the late planting season and the wetter weather, we also believe that some of the consolidation that's happened in the customers in that space as they continue with their integration efforts which includes looking at their fleets of boxes assessing their inventory levels and looking at their overall product requirements going forward is having some of the impact that we're seeing here.

I guess the last thing I'd say about what we're seeing in that space is, we have no indications to believe that this is a shift in demand for the products long-term. We remain very focused and confident in that space to maintain our leadership position in helping our customers in that area, solve problems and deliver to their customers.

Tyler J. Langton
Analyst, JPMorgan Securities LLC

Q

Got you. Perfect, thank you. And then Andrean, I guess I think in your opening remarks, I guess you said you were, I guess open or you know to capitalize on opportunities. Does that mean sort of during sort of the CEO search, I guess Myers would be willing to look at acquisitions or should we kind of think of that as somewhat on hold until the new CEO is announced?

Andrean R. Horton
Interim President & Chief Executive Officer, Myers Industries, Inc.

A

Thanks Tyler. So we're going to continue to evaluate opportunities in the acquisition area. We're obviously looking for acquisitions that complement our organic growth strategy. We've talked about looking at proprietary acquisitions. So those tend to have a longer process. You usually don't have an intermediary involved, you're usually dealing directly with the seller. There are times where you're persuading the seller to sell. So, just over all those take a longer time. But with the guidance of our board during this interim process, we will continue to look at proprietary acquisitions.

Tyler J. Langton
Analyst, JPMorgan Securities LLC

Q

Okay, thanks. That's helpful. And then I just Kevin finally on free cash flow, I know this quarter you've benefited from strong working capital gains after you saw some pressures in the first half. Give any thoughts on kind of what to expect for Q4 around that?

Kevin L. Brackman
Chief Financial Officer & Executive Vice President, Myers Industries, Inc.

A

Yeah. I think obviously the $22 million of free cash flow for the third quarter is not a sustainable quarterly amount because of the significant reduction in receivables that we had in the third quarter. What I would say though if you look at our year-to-date amount, $34 million over three quarters, so roughly $11, $12 million per quarter. I think that is a reasonable amount of free cash flow for us on a quarterly basis.

Tyler J. Langton
Analyst, JPMorgan Securities LLC

Q

Great. Thanks so much.

Operator: [Operator Instructions] Your next question comes from the line of Chris Sinnott with Cowen. Your line is open.

Christopher Sinnott
Analyst, Cowen & Co. LLC

Q

Good morning, and thanks for taking my question. I had a question about the Distribution Segment EBITDA margins. So, would the Tuffy acquisition not have affected the 10% EBITDA margin goal that you guys have of 10% by 2020 just this keeping that 10% where it is as the target imply any change to the underlying business margins or am I reading too deeply into it?

Kevin L. Brackman
Chief Financial Officer & Executive Vice President, Myers Industries, Inc.

A

I think you're probably reading too deeply into it. I – so we said the 10% EBITDA margin goal prior to acquiring Tuffy. So, we're sticking with that goal, that's still our goal. However, we are hopeful that Tuffy will be accretive to that margin.

Christopher Sinnott
Analyst, Cowen & Co. LLC

Q

Okay. That's helpful. Thank you. And if I could just squeeze in one more question about the dividend, it's a steady dividend, it's something that doesn't often get a lot of attention on these calls. But I'm curious about what you guys think your capacity is for ratcheting that up over time not necessarily next quarter or even the quarter after that, but the way the board looks out of the way current management is looking at it how a new CEO might think about. Any thoughts you have on the dividend going forward would be helpful? Thank you.

Kevin L. Brackman
Chief Financial Officer & Executive Vice President, Myers Industries, Inc.

A

Yeah. We review the dividend every quarter with our board and we will continue to do that in the future. What I would say is our focus for capital deployment in the near-term continues to be on the organic growth and M&A portions of our strategy. So, that's the focus in the near-term and we'll continue to look at the dividend with our board every quarter.

Christopher Sinnott
Analyst, Cowen & Co. LLC

Q

Great. Thanks.

Operator: There are no further questions at this time. I will turn the call back over to the presenters for closing remarks.

Monica Vinay
Vice President, Investor Relations & Treasurer, Myers Industries, Inc.

Thank you. We thank all of you for your interest in Myers Industries and your time and participation today. As a reminder, a transcript of this call will be available on our website within approximately 24 hours. A replay will be immediately available via webcast or call. Details can be found on the Myers Industries website under the Investor Relations tab. Thanks and have a great day.

Operator: This concludes today's conference call. You may now disconnect.