AMPCO-PITTSBURGH CORPORATION

Moderator: Masha Trainor
November, 02, 2015
10:30 a.m. ET

Operator: Good morning, my name is Blair and I'll be your conference operator today. At this time I'd like to welcome to Ampco Pittsburgh Corporate Third Quarter 2015 earnings conference call. All lines have been placed on mute to prevent any background noise. After the speaker's remarks there will be a question and answer section. If you would like to ask a question during that time, simply press * then the number 1 on your telephone keypad. If you would like to withdraw your questions, press the # key. Thank you.

Masha V. Trainor, Vice President, General Counsel, and Corporate Secretary, you may begin the conference.

Masha Trainor: Good morning everyone to the third quarter earnings calls. With me today are; John Stanik, our Chief Executive Officer; Dee Ann Johnson, Chief Financial Officer and Treasurer; Rose Hoover, President and Chief Administrative Officer; and Terry Kenny, president of Air and Liquid Systems Corporation. Before we begin, I need to make the following reminder regarding forward-looking information. Statements or comments made on this conference may be forward-looking statements and may include financial projections or other statements of the corporation's plan, objectives, expectations or intentions. The corporation's actual results may different significantly from those projected or suggested in any forward-looking statements due to a variety of factors, including those discussed in the corporation's most recently filed Form 10K. . We do not undertake any obligation to update or otherwise release publicly any revision to our forward-looking statement. I will now turn the call over to our Chief Financial Officer Dee Ann Johnson.

Dee Ann Johnson: Thank you Masha. Good morning everyone. Sales for the third quarter of 2015 were $58 million versus $65 million for the third quarter of 2014; a decrease of $7 million or 10.8%.

The decrease is primarily attributable to our Forged and Cast Engineered Products Group. Gross profit, as a percentage of net sales, was 16.2% for the third quarter of 2015 versus 18.6% for the third quarter of 2014. The decrease is due to lower production levels resulting in an under absorption of fixed costs and lower margins. Selling and administrative expenses were $8.7 million for the third quarter of 2015 in comparison to $9 million for the third quarter of 2014, a decrease of roughly $300,000 or 3%.

Other expense fluctuated primarily as a result of changes in foreign exchange gains and losses and lower costs associated with operations previously discontinued. While insignificant for the current year quarter, these combined costs approximated $400,000 for the prior year quarter. As of September, 30th, 2015, our estimated annual effective income tax rate is expected to approximate 40.1% compared to 31.6% for 2014. The increase is primarily due to favorable adjustments identified when filing our tax returns.

In summary, the corporation incurred a net loss for the quarter of approximately $1.5 million or $0.14 per common share versus a net loss of $343,000. or $0.03 per common share for the third quarter of 2014. From a segment perspective, sales for our Forged and Cast

Engineered Products segment decreased approximately $ 6.1 million or roughly 14% for the third quarter of 2015 compared to the third quarter of 2014. The decrease is primarily attributable to a lower volume of traditional roll shipments offset by a slight increase of other forging products.

An operating loss was incurred for the quarter due to the lower volume of shipments and under recovery of costs resulting from lower production levels and weaker margins. Additionally, weighted average exchange rates used to translate sales of our U.K. operations from the British pound sterling to the U.S. dollar were lower for the third quarter 2015 than a year ago which reduced sales by approximately $1.1 million . The change in the weighted average exchange rates did not have a significant impact on operating results for the current quarter.

Sales for our Air and Liquid Processing segment for the third quarter decreased by approximately $1.2 million or 5% primarily from a decline in sales of heat exchange coils due to a lower volume of shipments to the fossil fueled utility and industrial markets. Sales of air handling units decreased as a result of low order intake in the latter part of 2014 and first quarter of 2015. Sales of pumps increased due to a higher volume of shipments of commercial pumps to the power generation market. Operating income for the third quarter of 2015 for the segment increased however primarily due to product mix and cost containment.

Backlog at September 30th, 2015, approximated $143 million in comparison to $168 million at December, 31st, 2014; a decrease of $25 million or 15%. Backlog for the Forged and Cast Engineered Products group decreased $30 million as a result of lower demand from roll customers who continue to operate below capacity causing shipments to outpace new orders. Further impacting the roll business is the strong U.S. dollar and British pound sterling against most major international currencies, especially the euro. Backlog for the Air and Liquid Processing group increased $5 million and benefited from higher order intake for pumps and air handling units while orders for heat exchange coils decreased principally due to reduced activity in the fossil fueled utility and industrial market.

Regarding our balance sheet, cash and cash equivalent equaled $87.4 million as of September 30th, 2015 in comparison to $97.1 million at December, 31st, 2014, a decrease of $9.7 million. Accounts receivable decreased $8.2 million from year end primarily due to lower revenue in the third quarter of 2015 versus the fourth quarter of 2014 coupled with an increase in days sales outstanding due to the mix of customers, slower payments by customers, and longer payment terms granted to customers.

Inventories increased approximately $7.6 million at September, 30th, 2015 from December, 31st, 2014 primarily due to higher inventory levels for the Forged and Cast Engineered Product segment including higher raw materials to take advantage of reduced pricing and, to a lesser extent, delay in the deliveries of rolls. Employee benefit obligations decreased at September, 30th, 2015 from year end by approximately $8 million primarily as a result of the partial freezing of the U. S. define benefit pension plan in the first quarter of the year.

Moving on to cash flows, the corporation generated net cash flows from operating activities of approximately of $8.5 million for the current year period in comparison to $9.7 million for the comparable prior year period. The majority of the deterioration is associated with lower earnings. Net cash flows used in investing activities approximated $12.1 million for the 9 months ended September, 30th, 2015 versus the $10.1 million for the 9 months ended September, 30th, 2014 and included capital expenditures for our Forged and Cast

Engineered Product Segments and the purchase of certain assets of Alloyed Unlimited and Processing at the end of July for approximately $5 million.

As of 2015, we have commitments for future capital expenditures of less than $10 million with about half expected to be carried over into 2016. I will now turn it over to John.

John Stenik: Thank you Dee Ann.

Good morning, the third quarter was difficult for Ampco-Pittsburgh. Financial results were in line with expectations that I communicated to you during our second quarter call. UES or the Forged and Cast Engineered Product segment did not reach the level required to generate positive income, despite the partial benefit derived from our cost reduction programs. Orders from our two primary markets, the steel industry and fracking industry, continue to be weak in Q2 and at the end of Q1.

July was particularly disappointing resulting in a $1.2 million dollar or $0.12 per share loss. There were two expense items that also contributed to the third quarters' loss: acquisition related due diligence costs and an inventory write down. These two charges resulted in a $0.05 per share loss in the quarter. So if one does the math, the financial performance for August and September was positive despite the low sales. As has been the case all year long, our Air and Liquid Processing segment performed well and even exceeded our expectations for the third quarter by a small margin.

To review, the majority of the revenue for our Forged and Cast Engineered Products, occurs three or more months after receipt of an order. Orders from steel manufacturers were very light in March and continuing through part of July. Also, we try to hold price but this proved difficult to do and as you can see, our margins deteriorated by approximately 300 basis points from Q2. Similarly, orders for equipment that we began providing to the fracking industry dropped off significantly in Q2 as oil prices fell, resulting in lower demand for our products.

Since improvements, or recovery, in both of these industries is not expected for months, more restructuring must be completed in order for us to generate profit at the level of business that is available and at current market pricing. There will be more news about this in my fourth quarter call.

You will note that this is the first time I have mentioned our role in the fracking industry. Fracking operations consume certain forged equipment that we have begun to supply. In fact, fracking open dye forged products comprised a significant part of our market diversification strategy as we plan to utilize our forging manufacturing assets to participate in this sizable market. Valve locks alone are estimated to be as much $300 million in a typical year. Of course we will continue to supply forged and cast rolls globally. Little capital expense will be needed to branch into these new opportunities.

The third quarter was an important one for the corporation as we continue to progress in the turnaround of Ampco Pittsburgh Corporation, and there were significant achievements made. Most importantly, we completed our three strategic plan and received approval of it by our board of directors. The plan, which currently is based entirely on organic growth, provides for double digit revenue growth, a focus on R&D and new products, sales and marketing improvement programs, and continuing cost reductions especially in the area of manufacturing.

We have scheduled a meeting at the New York Stock Exchange next week, on November 10th, during which time my senior team and I will present a summary of this plan. The company continued to execute its previously identified cost reduction programs during the third quarter. For example, personnel at corporate headquarters were all relocated to our Carnegie, Pennsylvania office building from downtown Pittsburgh, 600 Grant St. Our lease for the old Grant St. occupancy will end in February 2016 and thus reduce costs at that time. On an annualized basis, savings derived from this one change will be approximately $700,000.

We continue negotiations with our Carnegie Plant United Steel Workers Union during the quarter. I believe both parties have worked hard in the past three months and negotiated in good faith. A tentative settlement has been reached and I hope that the contract will be ratified this week so we can move forward together. I believe that the Carnegie plant can play a vital role in our company's future growth.

We began the integration of our July, 29th acquisition, Alloys Unlimited and Processing Incorporated. Alloys Unlimited is a machining and distribution center for forged products located in Ohio. The operation was relocated in early August and I believe we have achieved normal operations in a relatively quick period of time. The employees have transitioned smoothly and quickly. No customer orders were missed. Now it's time to begin to growth this distribution center.

We continued to work on a new bank credit facility. It will be an asset based loan that will establish a level of credit with very few financial covenants. When combined with our cash reserves currently on our balance sheet, the credit facility will provide strategic flexibility allowing Ampco to take advantage of opportunities to improve its future performance through acquisitions and other investments. We expect the competition of the deal during the fourth quarter.

Currently, there are several opportunities to acquire companies in our strategic space. The conditions in our markets have been depressed for so long that I believe many quality companies are now in a weakened state or in search of strategy to create a better future. Ampco has identified attractive targets for merger and acquisitions and has pursued these targets during Q3. It is premature to discuss any details about these opportunities and I won't entertain any questions about them today.

However, I will say that I believe there is a number of ways that our company can become stronger, more flexible, and a more diverse integrated market force. Work is continued on the project to improve the financial performance of our Chinese joint venture. Currently, we are working on structural changes that should improve our market approach and our costs base. I hope the action plans can be completed in Q4. However, certain government approvals are needed in China and these may delay the end date into Q1 of 2016.

Looking ahead at Q4, at this time we expect revenue for Q4 to improve over Q3 and Q2 provided that our customers don't push orders that are currently scheduled for deliver into Q1 of 2016. That does happen sometimes. From an activity perspective, we expect Q4 to be extremely busy as we continue very important work and hopefully bring some of this work to a close, such as the new credit facility. There will be more expenses for consultant work for M&A activity and the bank deal.

Additionally, we will continue to execute our new action plans contained in our strategic plan. We will now take any questions.

Operator: At this time, I'd like to remind everyone in order to ask a questions, please press * with the 1 on our telephone keypad. Ampco Pittsburgh Corporation has asked that you please limit your questions during the Q&A session to one questions and then one follow up question. We will pause for just a moment to compile the Q&A roster.

Again, if you would like to ask a question, please press * with the number 1 on your telephone keypad. There are no audio questions at this time. I will now turn the call back over the presenters.

John Stanik: Well, hopefully next call we'll have more reason to talk. I expect our Air and Liquid Processing segment to continue to perform well. With respect to UES, or our Forged and Cast Engineered Product segment. It's going to be a difficult time extending into 2016 but we expect to stabilize the performance of this segment. We'll make many changes and many improvements.

However, since we do not project any substantial market improvements in our two key markets, steel and fracking for many months, I believe a major performance turnaround for the corporation may not be immediate. But it will occur at least as soon as our markets do and hopefully, sooner. All of the ingredients are in place or they will be within weeks. Much has been done in the last ten months and I continue to be truly excited about our corporation's future.

Thank you.

Operator: This conclude today's conference call, you may now disconnect.

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