AMPCO-PITTSBURGH CORPORATION

Moderator: Dora Gouveia
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Operator: This is conference # 56331713.

Operator: Good morning. My name is Alex, and I will be your conference operator today. At this time, I would like to welcome everyone to the Q4 2015 earnings conference call.

All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question and answer session. If you would like to ask a question during this time, simply press star then the number one on your telephone keypad. If you would like to withdraw your question, press the pound key. For those of you on the Stream, please take note of the options available in your event console.

At this time, I would like to turn the call over to Masha Trainor, Vice President and General Counsel. You may begin your conference.

Maria Trainor: Good morning, everyone, and welcome to our fourth quarter earnings call. With me today are John Stanik, our Chief Executive Officer; and Dee Ann Johnson, our Chief Financial Officer and Treasurer.

Before we begin, I need to make the following reminder regarding forward-looking information. Statements or comments made on this call may be forward-looking and may include financial projections or other statements of the corporation's plans, objectives, expectations or intention.

The corporation's actual results may differ significantly from those projected or suggested in any forward-looking statement, due to a variety of factors including those discussed in the corporation's Form 10-K. We do not undertake any obligation to update or otherwise release publicly any revision to our forward-looking statements.

I will now turn this call over to our Chief Financial Officer, Dee Ann Johnson.

Dee Ann Johnson: Thank you, Masha. Good morning, everyone. Sales for the fourth quarter of 2015 were $55 million versus $75 million for the fourth quarter of 2014, a decrease of almost $20 million or 26 percent. The decrease is primarily attributable to our Forged and Cast Engineered Products Group.

Gross profit as a percentage of net sales was 14.7 percent for the fourth quarter of 2015 versus 19.7 percent for the fourth quarter of 2014. The decrease is due to lower production levels resulting in an under absorption of fixed cost and lower margins.

Selling and administrative expenses were $11.9 million for the fourth quarter of 2015 in comparison to $10 million for the fourth quarter of 2014, an increase of almost $2 million. The increase is primarily attributable to acquisition-related transaction costs of $3 million, offset by lower selling cost, including commissions, driven primarily by the decrease in sales. Additionally, the fourth quarter of the prior year includes higher provisions for potential bad debts associated with an international customer of approximately $750,000.

During the current year quarter we received cash proceed of $14 million from an insurance carrier in rehabilitation. By comparison, in the fourth quarter of the prior year, the corporation recorded a charge of $4.5 million, which represented the net expense associated with extending the estimated cost of pending and future asbestos claims, net of any additional insurance recoveries for an additional two years, from 2022 to 2024. Both amounts are reflected as charge/credit for asbestos litigation in our fourth quarter press release.

Our statutory federal income tax rate is 35 percent. Our effective income tax rate for the fourth quarter of 2015 approximated 51.2 percent. The increase is principally due to the acquisition-related transaction costs incurred in the fourth quarter of this year, which are not-deductible for tax purposes. Instead, such costs are considered permanent differences and treated as basis of the assets to be acquired.

In summary, the corporation earned net income of $3.3 million or $0.32 per common share, which includes the after-tax benefit of $6.1 million or $0.59 per common share for the proceeds received from an insurance carrier and dissolution offset by acquisition-related costs.

By comparison, the corporation incurred a net loss of $2 million or $0.20 per common share for the fourth quarter of 2014, which included an after-tax charge of approximately $2.9 million or $0.28 per common share for the estimated increase in the cost of asbestos-related litigation, net of estimated insurance recovery.

From a segment perspective, sales for our Forged and Cast Engineered Products segment decreased approximately $16.3 million or roughly 31.3 percent for the fourth quarter of 2015 compared to the fourth quarter of 2014. The decrease is primarily attributable to a lower volume of traditional roll shipments and reduced selling prices. An operating loss was incurred for the quarter due to the lower volume of shipments and under recovery of cost resulting from the lower production levels and weaker margins.
Sales for our Air and Liquid Processing segment for the fourth quarter decreased by approximately $3 million or 13.1 percent when compared to the same period of the prior year. Sales of heat exchangers declined by approximately 16 percent, due to a lower volume of shipments to the fossil fueled utility and industrial markets, and Sales for pumps decreased by approximately 21 percent due to timing of customer delivery requirements.

Sales of air handling units increased by about 16 percent, principally on better order intake over the summer months. Despite the lower volume of sales, operating income for the fourth quarter of 2015 for this segment, excluding asbestos-related activity for each of the quarters, remained comparable.

Backlog at December 31, 2015, approximated $142 million in comparison to $168 million at December 31, 2014, a decrease of $26 million or 15 percent.

The majority of the decrease is associated with the Forged and Cast Engineered Products group, which decreased $25 million, due to a combination of lower demand from roll customers who continue to operate below capacity causing shipments to outpace new orders, as well as large customers placing orders quarter-by-quarter versus annually and the strong U.S. dollar and British pound against major international currencies, especially the euro.

Backlog for the Air and Liquid Processing group was down slightly from a year ago. The improvement in backlog for air handling units and pump helped offset the shortfall for heat exchangers.

Regarding our balance sheet. Cash and cash equivalents equaled $95.1 million at yearend in comparison to $97.1 million a year ago, a decrease of $2 million. Accounts receivables decreased $10 million from the prior yearend, due to lower revenue in the fourth quarter of 2015 versus the fourth quarter of 2014, offset by 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 $5 million at December 31, 2015, from December 31, 2014, primarily due to higher inventory levels for the Forged and Cast Engineered Products segment, including higher raw material levels, to take advantage of reduced pricing and to a lesser extent delays in the delivery of rolls.

Employee benefit obligations decreased at December 31, 2015 from December 31, 2014, by approximately $17.5 million, primarily as a result of freezing a substantial portion of the U.S. defined benefit pension plan during the year and an increase in the discount rates, which reduced the liability.

Moving on to cash flows. Cash flows generated from operating activities for 2015 and 2014 were comparable. Net cash flows used in investing activities approximated $14.3 million for 2015, and includes capital expenditures of roughly $9.5 million and the purchase of Alloys Unlimited & Processing earlier in the year for $5 million. As of December 31, 2015, we have commitments for future capital expenditures of less than $10 million, the majority to be spent in 2016.

I will now turn it over to John.

John Stanik: Good morning. The fourth quarter of 2015 was another difficult quarter for the company, as depressed market conditions for Union Electric Steel continued. Sales were down 26 percent year-over-year, as new orders were light and UES customers delayed several booked orders.

As a result of the light volume, fixed cost absorption was low in the fourth quarter. Low fixed cost absorption also had an adverse impact on gross margin for Q4, which was down 500 basis points year-over-year. Price compression also contributed to the decline in gross margin, as competitors continued to drop price in order to take share. Low revenue and low margin are very, very difficult combination to deal with.

I should also mention that M&A expenses for the Akers acquisition and U.K. severance expenses added approximately $3 million of cost to SG&A. The two bright spots for the quarter were the continued solid performance of the Air and Liquid Process segments and the asbestos insurance recovery, Dee Ann mentioned, equaling $14 million.

For the year, conditions in the steel industry and consequently UES's performance deteriorated further with each passing quarter. During the third and fourth quarters, several rolling mills were idled in the western part of the world, thus shrinking the size of the market for rolls. Additionally, in Q4, a few of our customers notified us that they were extending payment terms, which we believe will stress our networking capital values in the coming months.

Air and Liquid Processing was solid throughout the year. And I'm pleased to report that our air handling business showed significant financial performance. However, revenue overall declined for this segment, as spending by the coalfired power plants, a major market segment for us, was down dramatically throughout 2015 as compared to 2014.

For 2015, Ampco-Pittsburgh reported SG&A of roughly $40 million, an increase year-over-year of $2 million. However, if we exclude M&A expenses and the frozen defined benefit pension curtailment expense for the year, SG&A would have been down year-over-year by roughly $2 million or more than 5 percent.

These expenses as a percentage of revenue should decline further in 2016. However, additional M&A expense and synergy costs for the acquisition will be incurred during at least the first two quarters of 2016 and quite possibly into the third quarter.

While we got off to a great start in 2015 regarding open die forged engineered products, our diversification strategy didn't yield much benefit after Q1. For the year, revenue for open die forged products had nearly doubled versus 2014, from $13 million in 2014 to approximately $24 million in 2015. That's a very attractive increase.

But the business abruptly dropped off near the end of Q2, as the oil and gas market prices began to drop, and this market has not recovered to date. But we are very pleased about that growth rate that was exhibited in just the first five months of 2015.

Alloys Unlimited & Processing, our July 2015 small acquisition, has been integrated within our UES business and began to exhibit signs of growth, especially during the past couple of months. I continue to be very optimistic about our potential in this relatively new market, a diversified market for us, especially once oil and gas inventories decline and prices increase.

So looking at all of the information, there is not a lot of good news to report. But the important question is, what are we going to do about this situation, and the answer is planning. Most importantly, we will aggressively integrate the Akers acquisition and capture the $13 million to $15 million of synergies, as prudently, but also as quickly as possible. There will be one-time costs, but most of those should end, as I said, by the end of the third quarter of 2016.

In the meantime, we will optimize our collective operating assets, finalize our combined commercial approach and we'll do that before the end of March, and implement our performance products versus low-price products market strategies. The rapid implementation of the integration should significantly strengthen our position in the marketplace and in the near term.

Secondly, we'll continue to execute our strategic plan action items and track our progress versus our expected results, and we'll do that on a quarterly basis. As a reminder, our strategic plan is expected to result in increased profitability and double-digit compound annual revenue growth.

Some of these aforementioned strategic action items are lean manufacturing initiatives. They will focus on efficiency and productivity improvements, which will ultimately lower costs and improve margins. These operational changes will be implemented throughout the year with $2 million to $4 million of expected benefit to be secured in 2016.

Summarizing this, Ampco-Pittsburgh is not waiting for the steel industry or the oil and gas markets to strengthen. We intend to be profitable in the short term. We consider today's market conditions to be the new normal for our company, and we are positioning ourselves to be strong now. We will manage aggressively and be as dynamic and as flexible a company as possible.

I'd like to say a few words about the Akers acquisition. Our press release this morning announced the closing. I am pleased that our rolls will now be marketed under the very strong brand name of Union Electric Akers. The largest non-government roll manufacturer in the world, with two of the best performing, best technical offerings in the industry are now combined. As a reference, Akers revenue is roughly equal to UES's revenue.

With the acquisition, we have an enhanced geographic footprint, a more complete roll product portfolio and lower cost product offerings, which should position the combine companies for strong performance in the future. We have been preparing for the integration of the two entities for weeks now and are very ready to implement that integration.

Yesterday, there was another quite positive announcement and that was the United States issuing preliminary dumping duties on cold rolled coil, one of our major customer segments. Tariffs, at least preliminary anti-dumping tariffs, will be place on sources from seven countries. Some of these tariffs are extremely large.

For example, the duty on Chinese cold rolled coil will be 266 percent, Brazil 39 percent roughly and Japan approximately 71 percent. These are big numbers and hopefully they will have a quick and significant impact on our customer base in the United States.

Let's talk a bit about the dividend decision. We have continued to pay a quarterly dividend of $0.18 per share, even though the company's net income recently has been less than the dividend payout. Yesterday, Ampco's Board of Directors made the decision to reduce the dividend to $0.09 per quarter going forward.

With our customers extending payment terms, with so many opportunities in front of us such as our strategic capital plan and other potential acquisition targets, we believe this move is appropriate at this time and in the best strategic interest for the corporation.

However, I want to stress, this decision is not necessarily permanent. The Board is committed to review its decision on the dividend quarterly, and I will update shareholders during future quarterly calls regarding any increases or decreases in the future.

Q1 outlook. Obviously, there is a lot of very positive things being started at this point in time, but I think we're headed for a tough first quarter. Obviously, the lack of Union Electric Steel revenue and Union Electric Steel's low margins have been our principal problem areas, and I expect things will not change dramatically overnight. Air and Liquid Processing, though, is expected to continue to contribute to a solid and consistent performance.

During the beginning of this year, the Union Electric Steel revenue in January was quite low and the company recorded a loss. February revenue was considerably better than January, significantly in fact. But we don't yet know what our bottomline results will be.

I expect revenue for the quarter to be less than desired. Fixed cost absorption will again be a problem. And while I expect the cost reduction programs of last year will provide savings, there will be some or let's say more M&A costs and synergy costs in the first quarter that will offset those benefits.

Therefore, we believe a Q1 net loss is not only possible, but probable. However, bookings in February were stronger than late last year, and I hope this is a beginning of a trend which bodes well for future quarters.

That concludes my presentation, and we'll now take your questions.

Operator: At this time, I would like to remind everyone, in order to ask a question, please press star then the number one on your telephone keypad. I would like to also remind everyone to please limit your questions to one question and one follow question only. We’ll pause for just a moment to compile the Q&A roster.

Your first question comes from the line of Scott Blumenthal of Emerald Advisors.

Scott Blumenthal: Dee Ann, can you maybe give us an idea as to the price mix and volume for Q4 in the forged and cast roll segment?

Dee Ann Johnson: Yes. I could. I'd like to do it for the year. I have that information handy and it's relatively the same as in the latter part of the year. The lower volume of shipments impacted our operating results by about $4.8 million for the year.

And our weaker margins and under recovery of cost as a result of the lower production levels further affected earnings by roughly $7.2 million.

John Stanik: It's about a $12 million hit overall.

Dee Ann Johnson: Right. And we would have experienced that somewhat the last year, but not to the same magnitude.

Scott Blumenthal: And you've mentioned also in your prepared remarks, Dee Ann, some delays (in post-installments) and some Q4 shipments. Do you expect to pick those up in Q1 or are those kind of on indefinite hold, what's the outlook there?

John Stanik: Scott, I'll answer that question. I think that some will be recovered late in the first quarter. Certainly didn't happened in January, but some have been delayed even further. We expect to get them all. We expect that those customers will honor those shipments.

There weren't any significant number of them that were – for any of these closed rolling mills that I referred to in comments. So yes, we think we'll get them peppered in probably by the end of the first half of the year.

Operator: Your next question comes from the line of (Nick Mills) of Gabelli Company.

(Nick Mills): I was wondering if you could give more color around the tariff announcement yesterday in terms of how does that affect the outlook for your business and your customers' businesses? And if you think it will meaningfully change the bands of U.S. production imports?

John Stanik: Yes, so I think it will. I think that if you consider the Chinese tariff alone. And let's face it; speaking candidly here, the volume of shipments at a very, very low price from China has been a major problem, not only in the U.S., but in the entire western half of the world. 266 percent is, if not the maximum, it has to be very close to the maximum award. It should make it very, very difficult for imports to be competitive.

Furthermore, I think that the antidumping program, the tariffs that are collected, as it used to be when I was at Calgon. Those tariffs are distributed to the petitioners.

So not only should there be a positive impact from the fact that there will be less dumped product being sold into the United States, there should also be a sizable amount of cash benefit that will be provided to the petitioners at sometime in the future.

But what effect will that have for us? Well, I think it will be a trickle down effect. I think that it will take a little bit of time. But I think that, I would expect, I have no way of knowing this, but I would expect that our customers will be increasing prices dramatically, and probably bringing capacity on stream increasing their absorption of fixed costs, so they should be getting more profitable.

That will put less stress on their purchasing activities, and hopefully in a short period of time, it will allow their supply chain people, people such as, an opportunity to increase our price. We're certainly going to be monitoring the market very, very closely and be looking for and pressing for price increases in 2016.

Operator: Your next question comes from the line of Scott Blumenthal of Emerald Advisers.

Scott Blumenthal: Dee Ann, you're going to carry about $30 million of debt related to the acquisition that closed this morning, is that correct? And if so, any idea, can you disclose what the interest rate?

Dee Ann Johnson: The final debt value will actually be closer to $26 million, and I do believe we have disclosed the interest rate, which is 6.5 percent.

John Stanik: The deal moved a little bit, which is customary for deals, with respect to, let's call it, toing-and-froing on a net working capital peg. But the initial $30 million that was paid or will be paid today will be cash, so there will be no debt. This keeps us in a healthy cash position that I was referring to in previous calls.

The stock, of course, will be issued immediately, or if it hasn't been issued – it has been, Masha tells me, it has been. So the stock is out there. That leaves, as Dee answered, roughly at $26 million note as opposed to a $30 million note at 6.5 percent interest compounded annually, that will be collected in 2019, so roughly a $50 million upfront hit to company for the benefit of having this great opportunity.

Scott Blumenthal: And then my last question is, and I'm sure everybody out there is very curious, if you could talk about utilization at Union Electric and also at Akers, particularly since you seem to having out a fair amount of capacity in rolls in Western Pennsylvania?

John Stanik: We do. That's a good comment. For those of you who don't know one of the plants that we have acquired with the deal is located in Western Pennsylvania. It's a facility that used to be referred to as National Roll, it's in Avonmore. It is a cast roll specialty manufacturing plant, whereas you probably remember that all of our American assets are forged roll.

So for the first time in the company's history, it will have both forged and cast roll manufacturing capability in the United States. We will also for the first time in the company's history – no, maybe not in the first time in history, because we had a Belgium facility, but we're back to making forged and cast rolls in Europe.

Regarding the really important question about capacity, as you probably remember, we did not buy the French facilities from Akers. We did not buy the Belgium facility. We thought that we would not be able to maintain a high-enough operating capacity with those facilities, so we chose to not purchase them.

We made this acquisition – in our very early discussions with Altor, the seller, we said, we will only make this acquisition if our operating utilization will be very high. And we plan to keep that promise. We can't continue to have this fixed cost absorption problem.

So we're going to be aggressive in terms of keeping our utilization high. At this point, however, we need to get new orders booked larger than revenue sold. We haven't managed to do that, although we had a good February in bookings.

So I'm hoping with the combination of everything we're doing, with having more products now, with being in every geography, with having what we believe the right assets in the right place, that we're going to be able to get our utilization, at some point, hopefully in 2016, into the high-80s or maybe 90 percent level.

That was the internal goal we set for ourselves. We're not there yet. But we expect to get there. And if we do, we will no longer talk about fixed cost absorption problems and our margins will automatically go up.

Operator: Your next question comes from the line of Albert Sebastian from Prospect Advisors.

Albert Sebastian: Just a few items. Can you give us the cash, working capital, OPEB, and asbestos liability at yearend?

Dee Ann Johnson: Yes, our asbestos liability at the end of 2015 was approximately $170 million and that compares to the asbestos-related insurance receivables that we have on the books at the same point in time of roughly $125 million. So if you do the math that's a gap, or what we view as our responsibility, to be paid out over a number of years of roughly $45 million.

John Stanik: Yes. There was no change in the net liability, because the $14 million was a cash payment as opposed to a future insurance coverage. So go on with the others. There was a change in the pension in OPEB significantly.

Dee Ann Johnson: In response to your working capital question, and I'll get back to you on the others, trade working capital; combination of receivables, inventories, and accounts payable at the end of December was roughly $90 million. And that compares to about the same at the end of last year. Just a slight deterioration.

Albert Sebastian: And you said the cash was $95 million?

Dee Ann Johnson: Our cash, yes, was $95 million.

Albert Sebastian: And then the pro forma shares outstanding after the issuance for the Akers acquisition?

John Stanik: Roughly 12.1.

Dee Ann Johnson: 12.1.

Albert Sebastian: And just can you give us a little bit more granularity on the customers that requested in extension of payment. Obviously, I don't expect you to give any names, but can you just give us sort of the nature of those?

Dee Ann Johnson: It's a primarily in our forged and cast rolls group. As they're experiencing a slowdown in their production levels, they're taking a look at a way to preserve their cash. So they've gone to us and asked for an extension of payments terms. Year-over-year, typical –f

John Stanik: Actually, they didn't ask.

Dee Ann Johnson: Right, yes.

John Stanik: Let me put it in a different way, not to interrupt Dee Ann, she is giving you a correct answer. But it was the larger guys, the large steel makers and it was throughout the western and half of the world.

So as is usually the case, when one or more does this, it becomes a trend. And we're talking about an extension that in some cases is 60 days worse than normal circumstances, and 30 days worse than where we were a year ago, that's significant.

Albert Sebastian: And just finally, when do you expect the 10-K to be out?

Dee Ann Johnson: In another week or so, it will be filled when it's due, roughly by March 15. You had one other question, and if you wouldn't mind, I'd like to answer. You had asked what the outstanding liability was for our OPEB plans.

Albert Sebastian: Correct.

Dee Ann Johnson: And that is roughly $8 million to slightly north of $8 million at the end of the year. That came down by roughly 33 percent from the prior year. At the end of last year, it was $14 million. We were able to institute some planned amendments during the year, which provided a savings of roughly $4.5 million.

Operator: There are no further questions at this time. I'll turn the call back over to the presenters.

John Stanik: Market conditions continue to be rough obviously. However, I know we are making progress. Our strategy is in place, it's being executed, and management scrutinizes the progress on a very rapid and regular basis. The Akers acquisition is now behind us.

We're making moves already today in the first day. And integration should result in accretion soon. There is a lot of work to do, but we intend to do it all, and to do it all, as quickly as possible. Thank you.

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

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