# Ampco-Pittsburgh Corporation

## Fourth Quarter 2016 Results

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**CORPORATE PARTICIPANTS**

**Melanie Sprowson** - *Director, IR*

**John Stanik** - *CEO*

**Rose Hoover** - *President and Chief Administrative Officer*

**Mike McAuley** - *VP and CFO and Treasurer*

## PRESENTATION

**Operator**
Hello and welcome to the Ampco-Pittsburgh Corporation Fourth Quarter 2016 Results Conference Call. All participants will be in a listen-only mode. Should you need assistance, you may signal a conference specialist by pressing the star key followed by zero. After today's presentation, there will be an opportunity to ask questions. To ask a question, you may press star and then one on a telephone keypad. To withdraw your questions, you may press star and two. Please also note today's event is being recorded.

I would like to now turn the conference call over to Melanie Sprowson, Director of Investor Relations and Corporate Communications. Ma'am, please go ahead.

**Melanie Sprowson**
Thank you, Jaime, and good morning to everyone joining us on today's fourth quarter conference call. I'm joined by John Stanik, our Chief Executive Officer; Rose Hoover, President and Chief Administrative Officer and Mike McAuley, Vice President, Chief Financial Officer and Treasurer.

Before we begin, I would like to remind everyone that participants on this call may make statements or comments that are forward-looking and may include financial projections or other statements of the corporation's plans, objectives, expectations or intentions. These matters involve certain risks and uncertainties, many of which are outside of the corporation's control.

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 most recently filed Form 10-K and subsequent filings with the Securities and Exchange Commission. We do not undertake any obligation to update or otherwise release publicly any revision to our forward-looking statements.

A replay of this call will be posted on our website later today and remain available for two weeks following the conclusion of the call. To access the earnings release or the webcast replay, please consult the Investors section of our website at ampcopgh.com.

Now let me turn this call over to Mike, who will provide an overview of the company's financial performance for the fourth quarter.

**Mike McAuley**
Thank you, Melanie, and good morning, everyone. Before I begin my review of our fourth quarter financial results, let me remind our listeners today that the results for the fourth quarter and full year 2016 in comparison to prior year in our press release are significantly affected by acquisitions made this year of Åkers AB and certain of its affiliated companies completed in March 2016, and ASW Steel acquired in early November of 2016. In addition, we recorded two significant charges in the quarter, which I will highlight in detail as shortly. While our press release this morning provides commentary on both the quarter and year-to-date, I will focus my remarks today primarily on our Q4 2016 results.

Sales for the corporation for the fourth quarter of 2016 were $92.1 million. This compares to sales for the fourth quarter of 2015 of $55.3 million. Sales in the Forged and Cast Engineered Products segment doubled compared to prior year, driven primarily by the inclusion of the acquired Åkers and ASW businesses. Sales for the Air and Liquid Processing segment for the fourth quarter of 2016 increased nearly 5% versus prior year. I'll comment more on the business segment results in a moment.

Selling and administrative expenses were $14.4 million for the fourth quarter of 2016 in comparison to $11.9 million for the fourth quarter of 2015. The increase is primarily related to the addition of selling and administrative costs for the acquired businesses, including a reserve of $1.5 million for accounts receivable from a customer who filed for Chapter 11 bankruptcy protection in the fourth quarter of 2016, but offset in part by acquisition related costs in Q4 2015 of $3 million which were higher than those incurred in Q4 of 2016.

Depreciation and amortization expense of $5.5 million for the fourth quarter of 2016 is up $3 million versus the prior year, primarily due to the inclusion of the acquired companies. Our new heat treat facility at the Harmon Creek plant was also recently brought online.

Now let me get to the charges recorded in the quarter which investors will note on our P&L. First, during the fourth quarter of 2016, the company undertook a revaluation of the estimated costs of pending and future asbestos-related claims, net of additional estimated insurance recoveries, including extending the period for those measurements from 2024 until the end of 2026. The result was an increase in our net asbestos liability. This impact was partly offset by asbestos-related proceeds received from a settlement with insurance carrier in excess of the receivable estimated. The net of these two items resulted in a P&L charge of $4.6 million in the fourth quarter of 2016. In contrast, in the prior year quarter, we recorded a $14 million gain on asbestos-related proceeds received from an insurance carrier in rehabilitation.

Second, during the fourth quarter of 2016, the company recorded impairment losses of $26.7 million primarily related to the company's conclusion that the goodwill in its Forged and Cast Engineered Products reporting unit was fully impaired. This goodwill was attributable to the Åkers acquisition. The opening balance sheet of ASW Steel acquired in Q4 2016 had no goodwill or any other intangible assets. The resulting operating loss for the fourth quarter of 2016 was $39.8 million. This compares to operating income of $7.7 million in the fourth quarter of 2015 which included that $14 million asbestos insurance credit I mentioned a moment ago as well as approximately $3 million in acquisition-related costs. The current quarter operating loss also reflects continued weak market conditions in the rolled business and in our other forged engineered products business.

Compared to the fourth quarter of 2015, other expense net for the fourth quarter of 2016 exceeded prior year due primarily to higher interest expense of approximately $0.8 million related to the acquisitions of Åkers and ASW as well as higher foreign exchange losses of $1.3 million linked to the stronger U.S. dollar. Despite the large loss before income taxes, the company recorded a small tax provision rather than a benefit due to the full valuation allowances still in place for most of the corporation's entities having triggered a three-year cumulative loss position last quarter. We described this issue in detail on last quarter's call and press release.

As a result, the corporation incurred a net loss of $43.1 million or $3.51 per common share for the fourth quarter of 2016 which includes per share amounts of $2.17 for the impairment charge and $0.37 for the net asbestos charge. By comparison, the corporation's net income for the fourth quarter of 2015 was $3.3 million or $0.32 per share, but included $0.59 per share in the net benefit of last year's asbestos-related insurance recovery offset in part by the higher acquisition-related cost.

Now, looking at the detail of our operating segments, sales for the Forged and Cast Engineered Products segment for the three months ended December 31, 2016, doubled compared to the prior year level, driven predominantly by the inclusion of the acquired businesses, which added sales of $41.9 million for the current year quarter. This was partly offset by a decline in the volume of legacy cast roll shipments.

The segment recorded an operating loss for the quarter which was higher than the operating loss in the prior year, driven by the goodwill impairment. The current year operating loss is related to the excess capacity and the cast roll market including the acquired Åkers businesses and the previously mentioned $1.5 million reserve against a receivable from the customer who filed for bankruptcy protection in Q4. John will comment more on the cast roll market and our capacity plans there in a moment.

Sales for the Air and Liquid Processing segment for the three months ended December 31, 2016 rose nearly 5% compared to the prior year quarter. The change is driven primarily by higher shipments of centrifugal pumps which more than offset softer shipments of custom air handlers as well as lower sales of heat exchange coils to the coal-fired power generation market. This segment recorded an operating loss for Q4 2016 driven by the $4.6 million net asbestos charge I discussed earlier. This compares to operating income in Q4 2015 led by a $14 million credit for asbestos-related proceeds received from an insurance carrier in rehabilitation, which because of its potential insolvency were not included in the insurance receivables previously recorded.

Beneath these asbestos items, higher centrifugal pump shipment volumes, improved productivity and cost reductions across the segment more than offset the impact of the lower heat exchange coil volumes in underlying operations. Backlog at December 31, 2016, was approximately $234 million, a 65% increase from the $142 million in backlog at December 31, 2015, primarily driven by the acquisition of Åkers and ASW, which added about $89 million. Order intake improved for both our legacy Forged and Cast Roll businesses during Q4 2016 but was partly offset by unfavorable FX translation. Backlog for pumps and air handlers increased, but was partly offset by decreases in backlog for heat exchange coils.

Now, turning to the balance sheet, accounts receivable increased approximately $27 million at December 31, 2016 from December 31, 2015. The increase represents the inclusion of accounts receivables for the acquired Åkers Group and ASW Steel offset in part by lower legacy sales in Q4 2016 versus Q4 2015, improved collections as well as reduction from foreign exchange translation effects.

Inventories increased approximately $24 million at December 31, 2016 from year-end 2015. Inventory added from the acquired companies was partly offset by reductions in inventory in legacy roll operations due to lower business activity, successful efforts aimed at reducing inventory levels and a reduction from foreign exchange translation. Accounts payable at December 31, 2016 increased approximately $23 million from the balance as of December 31, 2015, primarily reflecting the balance of payables added from the acquired companies.

Cash and cash equivalents of $38.6 million at December 31, 2016 declined $56.5 million compared to the balance of $95.1 million at December 31, 2015. Some selected significant cash flows for the year included the cash portion of the Åkers acquisition purchase price which was approximately $29 million, the cash portion of the ASW acquisition purchase price which was $3.5 million, payment of dividends of $5.2 million, payment of asbestos-related liabilities of about $4.4 million, receipt of approximately $10.9 million from the settlement with an insurance carrier and capital expenditures year-to-date of approximately $11 million. CapEx for Q4 of 2016 was approximately $6 (million) to $7 million.

I will now turn the call over to John. John?

**John Stanik**

Thank you, Mike. Good morning. Although Mike has provided a thorough explanation of our financial results, I want to add some of my comments and perspectives. When evaluating the company's performance, I look at GAAP and non-GAAP results very closely. GAAP results of course are the reported numbers, but non-GAAP results remove all adjustments, write-offs, etc. What's left is very important because what I'm looking for is has the company moved forward and is it improving? The most significant impact for the corporation for the last five years has been the roll market decline. That’s how long demand has been in this decline and our products' price compressed. Five years. And there was further deterioration in 2016.

Cast roll demand, particularly in Europe, diminished significantly. This has had a big negative impact on newly acquired Åkers performance and was a large part of the story which necessitated the goodwill write-off. When studying the underlying results, we also see volume decrease in 2016 for our legacy forged roll business. There was lower than expected volume, some of which was due to lost business from price increase attempts. Air and Liquid systems had their challenges also; however, they were able to overcome these challenges for the most part and continue their consistent profitable performance.

So, what underlying positive exists, and what improvements did we make in 2016? Well, I have to begin with the acquisitions. I'm convinced and remain convinced that both Åkers and ASW provide a strong growth platform that should provide increasing profits beginning in the near future. I see further cost reduction accomplished, significant manufacturing efficiency improvements achieved, and for the last six months a growing order intake with increasing roll prices. And I see ASW and Union Electric Steel already working closely together to optimize short-term financial results and strategically develop our diversification program.

Allow me to get a little more granular. The decline in cast roll business availability reduced our operating income expectations by nearly $10 million; that's a big number for us. This problem was most pronounced in Europe. On the positive side, from a cost reduction and efficiency standpoint, there were numerous improvements. In our legacy business for both segments, cost reduction programs and efficiency improvements yielded more than $6 million in savings that should continue into the future.

During 2016, ASW reduced their costs by improving their melting efficiency by nearly 25%. For Åkers, the capture of the existing synergies of the acquisition totaled a gross level of $8 million with only $3 million hitting P&L after the costs involved obtaining those synergies, but that $8 million will continue into the future. Additionally, we expect to get at least $5 million more in synergies from that acquisition in 2017; however, of course there will be some cost associated with that new capture. And as I mentioned in my Q3 presentation, we have plans to increase our manufacturing utilization, thereby optimizing our overhead absorption and maximizing the operating efficiency of all of our operating roll manufacturing plants. In my opinion, this is real progress, and I'm very pleased with these accomplishments.

Let's talk a little bit about roll pricing. We announced a price increase early in the second quarter. For a period of time, our competition utilized that period as an opportunity to take share. Lost business impacted both the legacy forged and the new cast roll businesses; however, this announcement did serve notice that additional price decreases for our rolls were at an end. As time went on during the second quarter and early into the third, we received spotty improvements in price; however, in the fourth quarter there was more significant traction. Therefore, once fourth quarter contracts are fulfilled, which should begin mid-year 2017, we should see positive gross margin impact from price increases.

Before I move on to other topics, I think it's a good idea to have Mike explain to you our goodwill write-off to give you not so much an understanding of GAAP accounting practice, but why the write-off occurred. Mike?

**Mike McAuley**
Sure, John. Let me add little more color on the impairment charge we've recorded this quarter. First, like the asbestos charge in the quarter, this is also a non-cash charge. It represents primarily the write-off of goodwill in the Forged and Cast Engineered Products reporting unit resulting from the Åkers acquisition. In connection with our strategic planning process, the goodwill impairment test completed in the fourth quarter of 2016, we determined that the goodwill in the Forged and Cast Engineered Products

reporting unit was fully impaired primarily as a result of further depressed market conditions.

Despite no fundamental changes in the steel industry production generally, no fundamental change in the regulatory environment, no loss of major customers and having seen actually favorable changes in tariff regimes aiding western steel makers, the decline in the cast roll market since the acquisition as well as lower margins than we expected in the acquired Åkers businesses and slower demand in other forged engineered products were key factors in our assessment that the fair value of the Forged and Cast Engineered Products reporting unit was less than the carrying value and an enough so that the goodwill was fully impaired.

Back to you, John.

**John Stanik**
Thank you, Mike.  As Mike mentioned briefly in his presentation, there was also in increase in our asbestos balance sheet liability posted in the fourth quarter, and that may cause some of you pause. There's actually embedded some good news in that situation, so I'm going to ask Rose Hoover, Ampco-Pittsburgh's President and CAO, who is also our resident expert on this topic, to provide some clarity and further explanation on what this means, and she'll also be here to take questions about this topic at the end of the call.  Rose?

**Rose Hoover**
Thank you, John.  Beginning in 2006, in an effort to provide total transparency for our investors, we hired experts and began to include valuations in our financial statements of our projected asbestos liability and insurance recovery for that liability.  Those valuations are performed every year, but every other year we have updated them to run for a new ten-year period.  In 2016, those valuations were updated for the ten-year period 2016 to 2026.  This means that two years were added to that valuation from the previous one done in 2014 to 2024.  In addition, in fourth quarter of 2016 we entered into a settlement agreement with one of our excess insurers for an amount in excess of the estimated insurance receivable for that carrier, and it resulted in a gain.

The net of the two impacts, the valuation of the liability and the update of the insurance receivable, was a $4.6 million charge during the quarter.  Actual settlement and defense costs paid for the past five years show a 23% decline in those costs over that five-year period.  The corporation paid an average of $4 million a year over that same five-year period for costs not covered by insurance.  We retained experts who use accepted market studies and are able to estimate our share of the market for the continued filing of these claims.  Based on that analysis we are told to expect a continuation of a downward trend in a number of malignancies filed through the ten-year period.

**John Stanik**
Thank you, Rose.  So, just to reiterate what Rose just said, we are seeing a decline in the costs, and if you look at those five years, you would see that continuous consistent decline.

I'd like to now move over to a discussion about ASW's acquisition.  A very positive and strategic move for us in November was our acquisition of a specialty steel producer located in Welland, Ontario, named ASW Steel.  ASW was acquired for a total of approximately $13 million, including debt assumed.  With annual revenue of approximately CAD65 million, ASW is a relatively small company having approximately 130 employees.  It's located just across the Canadian border due north of Buffalo.  The company provides us with the broad cross section of metals chemistries that we need to expand our penetration into the open-die market.  This is a bolt-on acquisition, meaning that we don't expect any significant cost reduction synergies; however, and much more importantly, this capability positions Union Electric Steel to forge different materials and attack new different verticals in the open-die industry.

An example regards the recent strong resurgence in fracking block orders in the first quarter of 2017 that specifies stainless steel material. ASW makes various grades of stainless. Along with our new heat treat capital project that was completed in October, ASW is the last missing resource that we needed for our diversification plan. We had been looking at ASW for almost year and a half and liked their metals capability, so we initiated serious discussions a few months prior and closed the deal in November. The timing couldn't have been better. Already, Union Electric Steel and ASW are working on our growth strategy. In the few months since the acquisition, ASW has generated positive operating income for the company with the exception of December when they absorbed a $1.5 million reserve against receivables due to the declaration of Chapter 11 bankruptcy by a customer.

Roll market trends. A lot of positive change has occurred over the past few months. Steel pricing around most the world is up significantly and in some cases up hundreds of dollars per ton. Most of our large steel-producing customers are reporting a return to profitability. Roll purchases are up. Now, that's at the first time you have ever heard me to say that. Orders for cast rolls, which were so depressed in 2016, are up significantly, so much so that we have been compelled to delay the idling of our Avonmore, Pennsylvania manufacturing plant in order to meet delivery deadlines. But because we are not yet convinced that this is not a bubble, as a result of the cast roll inactivity of last year, we are proceeding with the idling of the melt shop on April 1st.

As a reminder, this plant was selected for idling due to its high cost, lower efficiency and non-competitive nature. At this time, it is unknown how long the idling may last, but we are still projecting months. Once we're convinced that the market demand for cast rolls is not a bubble and will be sustained we will reevaluate the idling of Avonmore.

With the stronger cash roll presence internationally that the Åkers acquisition provides us, we've been doing very well in increasing backlog of both forged and cast roll orders. As I mentioned previously, we are also getting price increases. While I hope there is more price to be obtained in time, I don't want to disclose our future pricing strategy, but I will say that I am quite encouraged by the progress that our sales force has made.

Now, I want to caution everyone to understand certain realities of the roll business. The majority of the rolls that we're manufacturing and shipping in the first quarter are from the orders we received late in the second quarter of 2016, and therefore don't reflect an increase in margin due to price increase. Any improvement in the gross margin in the first quarter will primarily stem from last year's synergy capture and cost reductions. We expect margin improvement due to price increases to begin to occur late in the second quarter. Additionally, volumes are up in Q1 year-over-year; therefore, our fixed cost absorption should be higher.

Let's talk a little bit about the frack block business. Fracking block inquiries have been much stronger than expected so far this year, and we have been quite successful receiving orders. As the vast majority of these block orders are for stainless steel as opposed to the historical prevalence of alloy steel, the ASW acquisition has dramatically improved our competitive positioning. If this level of activity continues, we could manufacture volumes well in excess of our strong performance in 2015.

Air and Liquid systems. Once again our Air and Liquid systems segment performed well in the fourth quarter and for 2016, achieving their operating income plan. The only issue in this segment was limited progress on the top line for Aerofin, our heat exchanger business, offsetting the coal-fired power industry market decline. Consequently, year-over-year sales for the entire segment were down slightly; however, I'm convinced that our current marketing strategies to replace the slowness in that market are taking hold and should show improvement in the second half of 2017. Meanwhile, the two other businesses in the segment are off to a strong start.

China MaSteel joint venture restructuring: The restructuring of our historically poor performing Chinese joint venture, Union Electric Steel MG Roll Company, was completed in November. The joint venture added a third partner, another Chinese roll manufacturer named Jiangsu Gongchang Roll Company. Now, the three owners, MaSteel Group Holding Company, Union Electric Steel Hong-Kong and Gongchang, have ownership positions of 34%, 33% and 33% respectively. We sold a portion of our equity and expect payments of approximately $2.5 million in installments to be completed over three years.

We are very familiar with Gongchang. They have become the day-to-day operator of the restructured joint venture; in fact, Ampco-Pittsburgh has a 24% indirect interest in Gongchang through another joint venture. The company has been profitable recently and is very competitive within China and beyond. I believe that the new structure will result in lower costs and increased competitiveness, ultimately providing profit and dividends for the three shareholders. As you know, we have been working on the restructuring for a long time, and I'm very pleased that it is now complete.

New product delivery: Behind the scenes the Union Electric Steel/Åkers combination has been working on delivering new high-tech products for the roll industry. Prototype test rolls have been installed for several months at a few steel manufacturers in the Western World, and they've had great performance success. We expect that a technical presentation of the performance results to the industry will be made in the second quarter with commercialization of one early in the third quarter, another product in the fourth quarter and a third product in the first half of 2018. Perhaps I'll have an update on our May call or if not, during our second quarter call.

So, let's now look ahead. Before we look ahead to the first quarter of 2017 and the remainder of the year, I'd like to point out that for those of you who have been owners of our stock since the beginning of my term, we've been on a two-year journey to turn around Ampco-Pittsburgh, to put a growth platform in place, to restructure the company to make it more competitive and more efficient, and to strengthen its overall capability within its markets while being introduced into new markets. 2016 was a very important year for the company. We truly became a stronger international roll producer. We secure the potential for penetration and to a very large open-die forged market through the second acquisition, ASW.

For two years, we've worked on lowering our costs, restructuring what we do and how we do it, bringing on new talent and developing new technology. At this time, I'm convinced that we have made major progress in all of these areas. Now with the potential for a cooperative market in both volume and price and with an effective diversification strategy to implement, a new Ampco-Pittsburgh should be on the verge of delivering positive performance. Obviously, I'm optimistic about the short-term future of the company as well as the long-term. What can we expect in 2017? Well, as long as the market continues to provide optimism in both metals and oil and gas, we expect to improve our performance over the year progressively.

At this time, I do not expect a profitable first quarter primarily because we're dealing with older orders that haven't included any price increase and low frac block shipments in January and February. The second quarter idling of Avonmore will have negative costs associated with lower fixed cost absorption and with the reduction in force due to various benefits that will be paid to the workers via the collective bargaining agreement that's in place; however, block shipments are expected to increase significantly from the first quarter. Heavy roll production is projected for all plants throughout the company, but it's too early to project financial performance for the quarter.

Summarizing, I expect that our financial performance in 2017 should show progress, much progress over the 2016 story that I talked about at the beginning of this call.

We will now take your questions.

**QUESTIONS AND ANSWERS**

**Operator**
Ladies and gentlemen, we will now begin the question-and-answer session. To ask a question, you may press star and then one. If you are using a speakerphone, we do ask that you please pick up the handset before pressing the keys to ensure the best sound quality. To withdraw your questions, you may press star and two. We do ask that you please limit yourselves to one question and a single followup. With those instructions in mind, once again, that is star and then one to queue in for a question.

And our first question today comes from Albert Sebastian from Prospect Advisors. Please go ahead with your question.

**Albert Sebastian**
Good morning, ladies and gentlemen. First question is I'm trying to understand the pricing. It seems as though you've initiated price increases and they have not been followed by your competitors. So, I'm trying to understand the industry dynamics here, why your competitors seem to be able to underprice you. In the roll business, is it strictly a commodity business or is there something that exists in the nature of the business that would allow one to charge a premium price due to the quality of the product or services or something else?

**John Stanik**
Well, I think that to address the second half of the question first, I think that the market conditions for our customers allowed them because of their reduced utilization of their manufacturing facilities to pursue commodity or low-performing roll purchases because they simply didn't need to run continuously at a high level of utilization. So, a company such as ours who can provide and has historically provided high-performing rolls is at a somewhat disadvantaged position from getting price increases. So that's the first point. However, there're still customers who of course do prefer higher performing rolls for less maintenance costs and longer performance.

What happened last year was we felt being such a large producer, especially in the western part of the world, that it was appropriate for us to take the lead when we announce the price increase early in the second quarter last year. We felt that it was very important to serve notice that we were not in a position because of the performance of the company to continue to offer price decreases. If you remember some of the things I said during the call when we announced that last year, we knew there were risks, and when you consider how depressed the market was in 2016 and how the cast roll business in particular took another step change downward in decline, our competitors were all struggling for volume.

And I suppose early in that period of time, they used that opportunity to get more fixed cost absorption and to take that business. But it began to change in the third quarter, and I think it began to change for a couple of reasons. I think that the most important reason was that the steel companies in the third quarter began to raise prices, the tariffs were put in place and prices began to increase everywhere, especially in North America, less so in Europe, but, and this is very important, also in Europe, including China. That trend, by the way, has continued. So, once our customers began to show profits and report profits and I think that began in the third quarter of some of them, I think our competition began to understand that they too could improve the situation for themselves and increase price.

At that time, we were already beginning to see, as I said in the presentation, spotty price increases. In the fourth quarter that began to change, and the price increases began to get more steady. In fact, price decreases in the fourth quarter were no longer requested, which was the first time in five years. So, I think it's a complicated story that took a period of time, but I think that now we're in a different situation than we were three quarters of a year ago and we can expect perhaps even more price increases as time goes on.

**Albert Sebastian**
Okay, let me just ask one other quick question on the ASW acquisition. What's the historical EBITDA or operating profit associated with that company?

**Mike McAuley**
Yes, Albert. This is Mike. We're not going to really want to disclose much below the segment level, but just to give you a feel, the company, ASW, when we made the acquisition they were profitable at the EBITDA level. I think we said that on the original disclosure, and we're seeing that as well currently a couple of months in here. With the exception of that receivable reserve that we took on an underlying basis, the company is still profitable at the EBITDA level.

**John Stanik**
Yes, but let me disclose a little bit more about that, Albert. ASW was in a very difficult financial position when we acquired them. They were owned by a couple of investors and their business was suffering from the same market, depressed conditions that the roll industry was suffering from.

Because of that sustained period of time, they were beginning to get into a debt position that was limiting them in getting working capital to grow and improve the business. That's why we were able to purchase them basically for $3.5 million plus assume their debt and provide them with working capital that has allowed them to grow. Since that time, since we have made the acquisition, we're seeing ASW surpass the business plan that we put together for them already, and we expect that to get even better probably mostly due to the stainless steel fracking block business that they are providing for us. They have a very attractive cost structure in terms of competition, and we expect them to begin to grow now that they have some working capital backing for that position.

**Albert Sebastian**
That’s very good. Thank you so much, John and Mike. Thank you.

**Operator**
Our next question comes from Michael Gaugler from Janney Montgomery Scott. Please go ahead with your question.

**Michael Gaugler**
Good morning, everyone. John, you had mentioned some positive comments on open-die forged market as it pertains to fracking, and I'm just wondering, when you look at where your shipments are headed in that market, are they primarily to oil and gas basins or are they primarily to gas such as Marcellus? And the reason I'm asking is the outlook for gas pricing looks relatively good and the rig counts have been improving across the board for both oil and gas, but the oil market’s looking a little weak at the moment. So, I'm wondering what your mix if you can share that is like.

**John Stanik**
Honestly, Mike, I don't know and can't give you a really good definitive answer on that. I can tell you that our orders are from a broad number of customers. I know that many of those if not all of those customers are selling to the drillers in shale deposits. So, I'll have an answer for you on the next call, but I can tell you that the speed with which this has happened and the fact that fracking has been going on over the

past couple years at a much reduced level, but it's still been going on, and there hasn't been a significant amount of block inventory replacement provided to these drillers. So, we're a little bit concerned that there may be a bubble here too where people are replenishing their inventory so that in the event that oil would continue to drop as it did last week that we expect that some of these ongoing and future shipments and orders would still occur. I think it's just too early, Mike.

**Michael Gaugler**
Understood; I'm not very...

**John Stanik**
But I'll give an answer for you.

**Michael Gaugler**
Okay. I'm not very concerned about a tail-off in oil because as you know, John, in your back market there is a lot of pipeline capacity coming online in Marcellus, many, many BCFs of gas to fill those pipes, and they have been moving forward on those projects, so that should be a net benefit even if oil weakens a bit as long as you're selling into that Marcellus market.

And then one other one, you also mentioned you were expecting gross margin improvements in the back half of the year, and I'm wondering if there is a way you can quantify that without giving formal guidance. When I look at your historical cost of sales, they're somewhere around the 80% level, and I'm just wondering, do they come down into the 75 or 70 level? Maybe on a basis points perspective what you're thinking the improvement could be in the back half of the year versus the first half?

**John Stanik**
No, it's a good question. I think that the fourth quarter except for all the noise that had to occur in December with the miscellaneous adjustments and write-offs that occurred that we were seeing an improvement over 2015 of about little more than 200 basis points. So, our cost reduction programs from '15 and the early ones in 2016 were starting to take hold, but that was all costs. If you consider the $6 million that I talked about that were of further cost reductions in the two segments and the potential for $8 million from the 2016 synergies, that's another $14 million, spread across the sales amount that's another $14 (million) divided by pick a number, 350, 400, just to be round numbers. That's another 3 percentage points. And then we're looking for price increase, and I really don't think I should talk about that, but it would be additional. So, if you add all those things together over the course of, let's say, 18 months beginning at the early '15, we should be talking about something that's considerably north of 500 basis points by the second half of the year from 2015.

**Michael Gaugler**
That's sizeable. That's all I had.

**John Stanik**
Well, we've been working hard.

**Michael Gaugler**
All right, thank you.

**Operator**
Our next question comes from John Walthausen from Walthausen & Company. Please go ahead with your question.

**John Walthausen**

Good morning. My question is about ASW iteration. You've articulated well how it's working well with Union Electric. The two questions I have are, how big a customer of ASW's is Union? I take it that was relationship that predated the acquisition, but you've talked about significant cost savings at Union post the acquisition. Can you explain a little bit how that works?

**John Stanik**
Yes, I think I understand the question. We were previously a customer of ASW, and we would get certain heats done by them for us primarily for the alloys that we were supplying into the fracking industry in 2015 and some of the products that we were trying to sell through Alloys Unlimited, our small business that we have in Ohio. So, there's been a fairly longstanding relationship, but the volumes that we were buying at those periods of time were relatively small.

Once we turned the corner for fracking this year and once the materials of construction for those blocks changed from an alloy steel to a stainless steel, we began to require a consistent weekly production of heats from ASW. ASW is also providing some of that same material for other people in the industry. In fact, they're a very solid, very good stainless steel provider in North America in general.

So, I would say that from 2016 prior to the acquisition to where we are now there's almost no comparison, we were probably—I can't give you a number of tons, but we are a significant purchaser of material. But where we expect to go in the future, and for the near future as we penetrate other verticals in the open-die industry hoping to be somewhat successful, we'll still be a very small player in that business, but what we lacked was a competitive supply of metal. In other words, for anything that we were going to try to accomplish in the open-die business, we were going to have to buy that metal and pay a profit to somebody else who was manufacturing it.

We liked ASW because we liked their cost structure and their competitive nature, and as you point out, we had a fairly longstanding relationship and knew the people well. We looked at a bunch of metals providers both in North America and internationally, and ASW is the one we chose. We think we got it for an incredible bargain price, and we expect to continue increasing the purchases that we at Union Electric Steel make from them. I hope that answered your question, John

**John Walthausen**
It does. The other part of the question, from your filings there's the snapshot of how they looked when you acquired them which is discouraging, but if I'm understanding it correctly and in spite of the fact that most small steel mills struggle and ASW seems to have had an on-and-off type of history, technically their ability to produce the grades of steel that you and other people want is at a good cost, is very good so that while the availability of the steel to you helps Union, if we just looked at it as a separate segment it would also be earning its cost of capital plus.

**John Stanik**
Yes, to run a mini-mill, to make steel like ASW does, there is a quite a bit of capital that's required. There is a fairly significant amount of maintenance. The price of scrap, even though it's low or has in recent history been quite low, there's still a lot of it required. So there is a substantial amount of working capital that's necessary.

The owners of the company since it restarted, and it restarted in approximately 2009, have been suffering through this long period of a weak market situation. So, I'm sure that there was a fatigue issue, and these investors no longer wanted to provide more capital. As a result of that, ASW was constantly near their debt limit. They had a credit arrangement, but they were bumping against it and they weren't producing the financial results that would encourage the banks to increase that limit. So, it was a catch-22 for them.

I think their business model was solid. I think we're going to prove that instantly or immediately, and with the little bit of help from metals, the metals industry in general in North America, I think that they have a real opportunity to grow and provide very positive results in and of themselves without the help of Union Electric Steel's frac block orders. So, if the fracking industry suddenly began to deteriorate, it would have a sizeable negative impact of course on ASW, but I do not think that it would necessarily mean that they would produce losses.

**John Walthausen**
Okay, that's helpful. And then the last question if I may was you mentioned in the roll business I believe three new product lines that you are introducing over the next couple of quarters. Can you give us a little bit more of an understanding of whether this is just sort of new products and the normal rate that Union, etc., has been introducing them or whether this is something that can meaningfully improve your competitive position?

**John Stanik**
Well, I think the latter part of the question remains to be seen. I'll characterize these new products as being products that have longer longevity than anything that is out in the market. So, based on the test results that we've been seeing, the company, Ampco-Pittsburgh and Åkers, have not really released new products that have had much of an impact in at least two years, actually for Ampco-Pittsburgh not in my entire term of two and a fourth years we haven't really released anything new.

The importance of new products of course is that they have sufficient performance improvement that we can charge a premium, and that's always been the criteria of success that I've set for Union Electric Steel and its R&D organization. Now that we have doubled the size of that organization and we have doubled the amount of money that we allow them to spend since the acquisition, these guys have been putting out some good work. These test rolls have been in place for I believe more than six months. So, this is an area where we expect positive benefits.

**John Walthausen**
Okay, good. That's very helpful. Thank you.

**Operator**
Once again, of you would like to ask a question, please press star and one.

Our next question comes from Justin Bergner from Gabelli & Company. Please go ahead with your question.

**Justin Bergner**
Good morning, John. Most of my questions have been asked. Just one last question, you talked about increasing price, but clearly as a consumer of steel, your costs are going up as well. Are these price increases that are going through merely the reflection of increasing steel costs on the input side or are they more than that?

**John Stanik**
Wow, let me think about that for a second. For input, things like scrap, transportation if oil prices go up etc., there is a standard practice in our industry which involves automatic surcharges. Those surcharges, while they may lag reality by three to six months, and these surcharges are becoming real at this point in time for scrap and not yet for transportation, but I think the answer to your question is they're real. The surcharges will cover the things you're talking about, and we should net the increases that we're getting.

**Justin Bergner**

Okay, that's great. And are you also seeing price increases in Europe or is mainly in North America that price increases are sticking?

**John Stanik**
We're seeing price increases everywhere, including Asia, and Europe.

**Justin Bergner**
Okay. John, that was it for me. Appreciate the call.

**CONCLUSION**

**Operator**
And, ladies and gentlemen, at this time, I'm showing no additional questions. I'd like to turn the conference call back over to management for any closing remarks.

**John Stanik**
Yes, thank you. I do have a closing comment. It's been a long two years for you, the shareholder, as well as for us. I've stretched the people here at Ampco-Pittsburgh to complete all the challenges that were set before them, strategic plans, multiple due diligences for real acquisitions and potential acquisitions, credit agreements, countless action plans to attack costs and efficiencies, and new training.

With much regret, I have to say there was a need for some loyal employees to leave the company during the restructuring. When one tries to accomplish a turnaround, it usually occurs in a down period. That's when turnarounds are needed. However, in my 13 years as a CEO, I have never seen a down market situation that seemingly introduced a new decline every year that had to be overcome, but I believe that we are very, very close to our goal of turning around the company. If we can enjoy just some sustained period of the current market activity, I have high hopes for the financial performance of today's Ampco-Pittsburgh Corporation. Thank you very much for your patience and for listening today.

**Operator**
Ladies and gentlemen, that does conclude today's conference call. We do thank you for attending today's presentation. You may now disconnect your lines.