

Ampco-Pittsburgh Corporation

First Quarter 2022 Earnings Conference Call

Tuesday, May 10, 2022, 10:30 AM Eastern

CORPORATE PARTICIPANTS

Melanie Sprowson - *Director, Investor Relations*

Brett McBrayer - *Chief Executive Officer*

Mike McAuley - *Senior Vice President, Chief Financial Officer and Treasurer*

Sam Lyon - *President, Union Electric Steel Corporation*

Dave Anderson - *President, Air & Liquid Systems Corporation*

PRESENTATION

Operator

Good morning and welcome to Ampco-Pittsburgh's first quarter 2022 earnings results conference call. All participants will be in a listen-only mode. Should you need assistance, please signal a conference specialist by pressing "*" "0".

After today's presentation, there will be an opportunity to ask questions. To ask a question, you may press "*" "1" on a touchtone phone. To withdraw your question, please press "*" "2". Please note this event is being recorded. I would now like to turn the conference over to Melanie Sprowson, Director of Investor Relations. Please go ahead.

Melanie Sprowson

Thank you, Joe, and good morning to everyone joining us on today's first-quarter 2022 conference call. Joining me today are Brett McBrayer, our Chief Executive Officer, and Mike McAuley, Senior Vice President, Chief Financial Officer, and Treasurer. Also joining us on the call today are Sam Lyon, President of Union Electric Steel Corporation, and Dave Anderson, President of Air & Liquid Systems Corporation.

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 statements due to various factors, including those discussed in the corporation's most recently filed form 10K 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. To access the earnings release or the webcast replay, please consult the investor section of our website at ampcoPGH.com. With that, I will turn the call over to Brett McBrayer, Ampco-Pittsburgh's CEO. Brett?

Brett McBrayer

Thank you, Melanie. Good morning and thank you for joining our call. As shared in today's press release, Ampco-Pittsburgh recorded a net income of \$1.6 million in our first quarter of 2022. The execution of price increases and expanded surcharges in our Forged and Cast Engineered Product segment was instrumental in helping Ampco-Pittsburgh return to profitability.

From a topline perspective, our sales increased by 9% from the prior year; demand remains strong for our products. Our backlog increased 36% versus the prior-year period and 12% versus the prior quarter. Despite the challenges we continue to face from an inflationary and supply chain standpoint, we will continue to focus on areas of the business we can control to further improve our performance.

The transformation of our North American fixed assets in our Forged and Cast Engineered Product segment is on track. The installation of the first pieces of our new capital equipment begins late in the second half of this year. With an expected continued ramp-up in working capital and related ongoing inflationary pressure we recently announced we are exploring options to obtain incremental capital to better enable us to capture topline growth opportunities

and position ourselves for higher profitability while we manage through the heavier CapEx spending phase of the equipment modernization.

From a safety and health perspective, we saw positive progress in our injury rates during the quarter. We will continue to drive further improvements as we remain focused on zero injuries in our workplace. I will now turn the call over to David Anderson, President of Air & Liquid Systems, for comments on the segment's performance. Dave?

Dave Anderson

Thank you, Brett. Good morning. Air & Liquid Systems' backlog ended the first quarter at a historic high, with backlog levels increasing 50% over the past six months achieving levels 27% higher than the prior quarter, and our Buffalo Air Handling business receiving its most significant order in decades.

Sales declined for the quarter primarily due to lower shipments of centrifugal pumps and custom air handling units. We continue to experience supply chain-related issues, including extended lead times on materials and customer-requested deferrals. While these supply chain issues have impacted our business, they are short-term in nature and do not impact the long-term strategic direction of the business.

Operating income increased compared to the prior year primarily due to an employee benefit change. Lower sales were partially offset by favorable margins and product mix. As we move forward, all three business units continue to implement new growth strategies, and we are seeing positive momentum in sales quotes and orders in the majority of the markets we serve.

Brett McBrayer

Thank you, Dave. I will now turn the call over to Sam Lyon, President of our Forged and Cast Engineered Product segment. Sam?

Sam Lyon

Thank you, Brett, and good morning. The segment's backlog increased 7.5% for the first quarter of 2022 and is at our highest level since February 2020. Backlog has increased approximately 30% from the pandemic trough in March 2021.

As stated on our last call, the first quarter was very strong for our non-rolled product line. We also anticipate an improved rolled sales mix with increased large forged rolled sales starting in Q3 of 2022 and continuing into 2023. Inflation continued to impact operations in Q1 2022. Materials and energy prices have remained elevated, and energy prices in Europe continue to be volatile.

We have seen the natural gas day ahead pricing in the UK fall from a high of \$85 per MCF in March to under \$10 per MCF today. This is compared to historic typical levels of \$11 per MCF in 2020 and \$19 per MCF in 2021. Futures for Q3 and Q4 are still elevated at near \$30 per MCF.

The United States natural gas has remained elevated at more than double the previous levels from around the midpoint of 2021. While we have seen an increase in fuel costs at our plant in Sweden, the overall energy cost is still less than half of our UK plant. Key alloys and inputs such as ferrochrome, scrap, and nickel have increased over 100% in the quarter due to the conflict between Ukraine and Russia. All other costs remain elevated.

As I have discussed before, our surcharge mechanism has some lag compared to actual cost. Our modified surcharge mechanisms to address the energy and transportation costs are now in place for most of our customers. In addition to surcharge expansion base pricing has been increased to address other general inflationary pressures, with the typical increase ranging from 5% to 7% over 2021 base pricing. We continue to monitor developments and costs daily and react where possible to minimize the effects on our business.

As Brett stated, our expansion and modernization programs for our U.S. plant assets continue on schedule. We are excited about these investments as they will provide a lower cost structure in our roll business and further growth in the nonroll business, which is currently at capacity. The oil patch continues to be strong, and we expect our shipments to remain solid in this market. We expect to complete our CapEx program by the middle of 2023. I will now turn it back over to Brett.

Brett McBrayer

Thank you, Sam. At this time, Mike McAuley, our Chief Financial Officer, will share more detail regarding our financial performance for the quarter. Mike?

Mike McAuley

Thank you, Brett. Ampco's net sales for the first quarter of 2022 were \$94.4 million, an increase of approximately 9% compared to net sales for the first quarter of 2021, primarily due to growth of 18% in the Forged and Cast Engineered Products segment.

Net sales for the Air & Liquid Processing segment in the first quarter of 2022 were 16% lower than the prior year period due to supply chain issues impacting the availability of components for production and customer delivery timing. Income from operations for the first quarter of 2022 was \$1.2 million. This compares to income from operations in the prior-year quarter of \$0.9 million. The current quarter's results include a \$1.4 million benefit from a change in certain employee benefits, most of which benefited SG&A expense.

The Forged and Cast Engineered Product segment's operating results declined slightly for the first quarter of 2022 compared to prior year, primarily due to a lower volume of mill roll shipments though this was partly offset by the favorable impact of the employee benefit change in the current quarter. While the segment continues to experience inflationary pressures, a significant portion of cost increases was recovered by surcharges and higher pricing.

Air & Liquid Processing segment's operating income improved slightly for the first quarter of 2022 compared to prior year despite the lower volume of shipments for the reasons Dave described. Other income expense net increased for the first quarter of 2022 when compared to the prior-year quarter primarily due to changes in foreign exchange.

At the bottom line, the corporation reported net income attributable to Ampco-Pittsburgh of \$1.6 million or \$0.08 per diluted share for the first quarter of 2022 compared to net income of \$0.2 million or \$0.01 per diluted share for the first quarter of 2021. Backlog at March 31, 2022, of \$327.5 million increased approximately 12% from December 31, 2021, and increased 36% from March 31, 2021. Backlog for the Forged and Cast Engineered Product segment improved 7% sequentially. This increases principally a result of increased orders for forged rolls due to improved demand for the segment's flat rolled steel and aluminum customers. Backlog for the Air & Liquid Processing segment is a record high and increased 27% sequentially, with backlog for each product line improving.

Net cash flows used in operating activities was approximately \$16.3 million for Q1 2022 due to an increase in trade working capital associated with a higher level of business activity and for inventories, higher costs associated with inflation, and supply chain disruptions.

Capital expenditures for the first quarter of 2022 were \$3.4 million, primarily for the Forged and Cast Engineered Product segment. At March 31, 2022, the corporation's balance sheet and liquidity position included cash on hand of \$6.8 million and undrawn availability on our revolving credit facility of approximately \$33 million.

Operator, at this time, we would now like to open the line for questions.

QUESTION AND ANSWER

Operator

We will now begin the question and answer session. To ask a question, you may press "*" "1" on your touchtone phone. If you are using a speakerphone, please pick up your handset before pressing the keys. If at any time your question has been addressed and you would like to withdraw your question, please press "*" "2". Please limit yourself to one question and one follow-up. At this time, we will pause momentarily to assemble our roster.

Our first question comes from Justin Bergner with Gabelli Funds. Please go ahead.

Justin Bergner

Good morning Brett; good morning, Mike. A couple of questions. You started off, I think, in your opening comments by saying that you were sold out in non-rolled product lines in Forged and Engineered Products just I wanted to verify that and what sort of sales level does that represent, and when do you expect to have the capacity to handle a larger sales volumes in non-rolled product lines?

Mike McAuley

Hey, Justin, it is Mike. In the quarter, we had about \$15 million in sales for our Forged Engineered Products, and I think I will let Sam comment on this, but I think what we mean by being sold out is we are capacity limited on our heat treat asset capability and so there's a limit to how much we can take and process over time based on the limitation in heat treat, but I will let Sam comment on that further.

Sam Lyon

No, that is accurate, Mike, and we expect DEP approval for construction this summer, and then we will install and be on track for the middle of next year to increase that capacity.

Justin Bergner

Okay. And I guess if I recall, you know before the push into non-rolled product lines or to expand the non-rolled product lines, you are doing about \$30 million annualized, so does that \$15 million of sales sort of suggest that you have doubled that annualized pace?

Sam Lyon

That's a little tricky because, volume-based, we are on track to what we said, but the inflationary situations with nickel and scrap and everything else have pushed the surcharge mechanisms and price up quite a bit. For example, nickel or 15-5 and 17-4 which are used for frac blocks that raw material has gone from like \$1.10 to \$2.10 a pound starting materials, so the volume is on track to what we said, but the revenue is higher.

Justin Bergner

Okay. And when you say the volume is on track to what you said just if you could remind us.

Sam Lyon

Well, the \$30 million of equivalent sales back then that is what we are producing. This year's plan was higher at \$38 million. We did roughly \$30 million last year, and then it goes over \$50 million last year and with past pricing.

Justin Bergner

Okay. Got you. All right, and then the \$1.4 million offset on the employee benefit change is that just sort of like a one-time item, is it non-cash, or is it sustainable savings?

Mike McAuley

It is a one-time item, Justin. It was non-cash; it really has to do with the policy that we changed regarding vacation benefits which in the past had been earned as soon as the clock turns to January one of the next year, and we amended our policy to make vacation be earned ratably throughout the year as the year progresses rather than have it fully earned as soon as the new year starts.

Justin Bergner

Okay. And then sort of where do you stand on price cost? I notice, I think I recalled you saying in the opening comments that a good portion of the higher cost in your Forged and Engineered Products segment was recovered. When do you expect to sort of get to full sort of dollar for dollar recovery in that business?

Sam Lyon

Well, there is, you know, a 2 to 3-month lag, and so you need the raw material pricing to level for that period of time, and then we will be on par or caught up with the surcharge mechanism will be reflecting the prices of the raw material. But we need prices to stabilize for that to happen.

Justin Bergner

Okay. And then sort of any update on what you are thinking in terms of the financing efforts in terms of what it would enable you to do assuming you go forward with some form of financing that you wouldn't otherwise be able to do with your balance sheet?

Mike McAuley

Yes, I can answer that, Justin. What we are thinking about is with the confluence of the events here where we have a ramp up and working capital to meet growing demand for our products and inflation, which is affecting that investment required in the growth in working capital and the fact that our CapEx timing is really--I mean we only spent like \$3 million in the first quarter it will be something similar in their second quarter and our plan is for about \$20 million in CapEx for the full year so our CapEx is going to start getting heavier in Q3 and Q4, and while we have plenty of space on the credit line at the moment, we are cautious of having to think about allocating, rationing anything having to do with taking orders.

And you know with the conflict in Ukraine and other things like that and the growth and our order book in both segments, we know there's more opportunity, and we want to be able to capture that opportunity.

Justin Bergner

Okay, thank you.

Operator

Again, if you have a question, please press "*" "1". This will conclude our question-and-answer session. I would like to turn the conference back over to the Chief Executive Officer, Brett McBrayer, for any closing remarks.

CONCLUSION

Brett McBrayer

Thank you. I am encouraged by our progress over the past quarter, and I want to thank our employees for their hard work and dedication. Our workforce continues to be the key to our success. I also want to thank our shareholders and our Board for your continued support.

We are excited about the future prospects for Ampco-Pittsburgh, and we are committed to driving improved performance in 2022 and beyond. Again, thank you for joining our call this morning.

Operator

The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.