Operator: Greetings, and welcome to the Columbus McKinnon Corporation First Quarter Fiscal Year 2020 Financial Results. [Operator Instructions] As a reminder, this conference is being recorded.

It is now my pleasure to introduce your host, Deborah Pawlowski, Investor Relations for Columbus McKinnon. Ms. Pawlowski, you may begin.

Deborah Pawlowski: Thanks, Doug, and good morning, everyone. We certainly appreciate your time today and your interest in Columbus McKinnon.

Joining me on the call are Mark Morelli, our President and CEO; and Greg Rustowicz, our Chief Financial Officer. You should have a copy of the first quarter fiscal 2020 financial results, which we released this morning before the market. If not, you can access the release as well as the slides that will accompany our conversation today at our website, cmworks.com.

If you'll turn to Slide 2 in the deck, I will first review the safe harbor statement. If you are aware, we may make some forward-looking statements during the formal discussions as well as during the Q&A session. These statements apply to future events that are subject to risks and uncertainties as well as other factors that could cause actual results to differ materially from what is stated here today. These risks and uncertainties and other factors are provided in the earnings release as well as with other documents filed with Securities and Exchange Commission. These documents can be found on our website or at www.sec.gov.

During today's call, we will also discuss some non-GAAP financial measures. We believe those will be useful in evaluating our performance. You should not consider the presentation as additional information in isolation or as a substitute for results prepared in accordance with GAAP. We have provided reconciliation of non-GAAP measures with comparable GAAP measures in the tables that accompany today's release and the slides for your information.

So with that, if you would turn to Slide 3, I will turn it over to Mark to begin. Mark?

Mark Morelli: Thanks, Deb, and good morning, everyone.

First quarter of Fiscal 20 is further evidence that our Blueprint for Growth strategy is expanding margins and driving earnings power.

Net income for the quarter was up 141%. On an Adjusted basis, earning per diluted share was up nearly 10%.

Margin expansion continued to drive earnings growth. This validates the effectiveness of our Blueprint for Growth strategy and the deployment of our business operating system, which we call E-PAS™ or Earning Power Acceleration. E-PAS provides the tools we use to execute our plan.

Since implementing E-PAS in 2017, we have consistently expanded margins, and ROIC. In fact, we achieved record adjusted EBITDA margin of 16.7% this past quarter, surpassing last year's previous record by 100 basis points. We made solid progress on ROIC as well, which reached 11.5%.

We had record gross margin, up 10 basis points from the prior record last year, as pricing more than offset tariffs and inflation. Contributing to the improvement was $500 thousand dollars in savings from the consolidation of our Ohio facility.

The simplification of our business, with Phase Two of the Blueprint for Growth strategy, is reducing our cost structure and improving our operating leverage. We had outstanding operating leverage for the quarter, as adjusted operating income increased on a lower revenue base due to divestitures. After adjusting for divestitures and the changes in foreign currency exchange rates, operating margin expanded 140 basis points to more than 13%.

Looking to slide 4, we are doubling down on Phase Two of our strategy this year. This phase is focused on Simplifying the Business, Operational Excellence and Ramping the Growth Engine. Our efforts continue to deliver results and we believe there is significant runway for further improvements.

Simplifying our business continues to drive earnings growth. In fact, $3.4 million dollars in operating profit in the quarter was from the 80/20 Process, an important tool in our operating system to help us simplify the business. There was also $1 million dollars of RSG&A savings delivered by our more streamlined organizational structure. Additionally, operating margin increased by 30 basis points as a result of the divestitures identified during our simplification process.

On the Operational Excellence side, our better cost discipline is improving our cost structure. During the quarter, we realized a 150 basis point reduction in RSG&A as a percent of sales. The combination of simplification and operational excellence is driving our efforts to reduce our operating footprint. In addition to divesting non-core businesses, we were able to consolidate into one facility in Ohio. As I mentioned earlier, this provided $500 thousand dollars in savings in the quarter and we are on track to achieve $2 million in savings this fiscal year. We are also moving forward with the consolidation of our footprint in China that we announced at our investor day. We expect this to cost about $1.5 million and to have about a one-year payback.

We are encouraged by the progress we are making in ramping our growth engine as well. I have met recently with several of our key accounts. Both Columbus McKinnon and our customers are seeing mutual growth opportunities, and our engagement is paying off. Several accounts in the U.S. and the Middle East are realizing strong growth as they penetrate new markets.

Product innovation is also ramping our growth engine and expanding addressable markets. Through product innovation that focuses on safety and productivity, we expand our markets and increase our opportunities to grow at higher margins. Let me give you a couple of examples.

We expect to accelerate sales of our new wire rope hoist platform with the recent launch of Crane Kits. Customers can now use our on-line configurator, which we call Compass, to enter basic design parameters and configure a standard crane package. For many customers, a basic industrial crane fits their needs. Our online system now allows them to get the crane designed, quoted, and delivered, quickly and easily with all components included. This allows our customer to be more productive as this reduces their engineering effort and shortens lead times for delivery and installation.

We are also expanding our addressable market and enhancing our position as a Lifting Specialist by launching a new offering for explosion-proof cranes. Our Stahl brand is a leader in explosion-proof cranes and now has certification in the U.S., allowing us to compete more effectively in the LNG and petrochemical industries.

Smart Movement is a key element of our growth strategy. We are the sole provider of a Magnetek brand, four-quadrant digital DC drive that improves safety and incorporates diagnostics. This digital drive is an ideal solution for older cranes that have DC motors and upgrades them to a digital system.

This retrofit to existing cranes, allows for many features of a modern crane - offering greater productivity and safety. This drive is helping us to grow with retrofits in the Steel and Waste-to-Energy market segments.

With that, let me turn it to Greg to cover our financial results. Greg?

Gregory Rustowicz: Thank you, Mark, and good morning, everyone.

On slide 5, net sales in the first quarter were $212.7 million dollars. As you know, we completed three divestitures last fiscal year which reduced sales in the quarter by $11.1 million. Foreign currency continues to be a headwind which also reduced our sales by $5.1 million compared to the prior year. We expect the headwind to continue in our fiscal second quarter. At today's foreign exchange rates, the headwind will be about 1%. Adjusted for FX and the divestitures, we saw good organic growth of 1.8%. Our pricing power was evident as we saw pricing improve by 1.8%. This included some of the benefit from our 80/20 process. Sales volume was up 10 basis points. We saw good growth from our project businesses, but a slowdown in our short cycle businesses which sell through distribution. We think the channel is managing inventory levels given the uncertain macroeconomic environment.

We saw solid growth in the quarter, particularly in the U.S. where sales increased $2.8 million or 2.5% adjusted for divestitures. Sales outside of the U.S. were up $1.1 million or 1.1 percent adjusting for the effects of the divestitures and foreign currency translation.

We think that organic growth of approximately 2% in the quarter was good performance given the macroeconomic uncertainty and simplification efforts that eliminates bad revenue. This reflects the progress we continue to make with customer responsiveness and ramping the growth engine. We believe we are growing share in key markets and executing well.

On slide 6, we achieved record gross margin of 35.5% in the quarter. This is a 10 basis point expansion in gross margin from a year ago and this is our ninth consecutive quarter of year over year margin expansion. As Mark mentioned earlier, the 80/20 process was accretive to gross margins. In addition, our pricing, which has an 80/20 element to it, is more than covering raw material inflation and tariffs. We feel that phase II of our strategy still has a lot of runway to further improve gross margins going forward.

Let's now review the quarter's gross profit bridge. First quarter gross profit of $75.6 million decreased by $4.0 million dollars compared to the prior year. This was largely a result of foreign currency translation, the divestitures and sales mix. We did see gross profit expansion from pricing net of material cost inflation, and productivity. Pricing net of material cost inflation contributed $2.5 million and productivity contributed $200 thousand of gross profit. Tariffs had a negative impact of $600 thousand dollars in the first quarter. In fiscal 20, with current tariff schedules, we expect tariffs will have about a $3 million negative impact on gross profit. We are actively working to mitigate this headwind. I will also point out that we incurred ($0.5) million of cost for the Ohio plant consolidation. This project is now complete and we expect to benefit by approximately $2 million in overhead cost savings in fiscal 20. Foreign currency translation reduced gross profit by ($1.6) million this quarter. The three divestitures negatively impacted gross profit by ($1.8) million and sales volume and mix was negative $2.8 million as we had lower volumes in certain of our project businesses and a higher level of rail projects this quarter.

As shown on slide 7, RSG&A was $45.1 million in the quarter or 21.2% of sales. This is a reduction in RSG&A of $6 million and an improvement of 150 basis points as a percent of sales from the previous year. The prior year first quarter included pro-forma costs totaling $1.6 million and the divestitures reduced RSG&A by $1.1 million. In addition, FX was a benefit in the current year of approximately $1.1 million.

The remaining reduction in RSG&A is a result of the simplification part of our strategy where we reduced SG&A by $1 million a year ago. We are also exercising good cost discipline as we look to drive our earnings power. We are forecasting our second quarter RSG&A to be about $46 million dollars.

Turning to slide 8, normalizing for the divestitures, Adjusted Income from operations grew 8.7% to $28.1 million or 13.2% of sales, a 140 basis point improvement over the prior year. Our adjusted operating leverage in the quarter was strong as Mark discussed, which reflects our ability to execute on our strategy to drive earnings power. Phase II of our Blueprint Strategy which includes Simplification, Operational Excellence and Ramping the Growth Engine are all contributing to driving our earnings power.

As you can see on slide 9, GAAP earnings per diluted share for the quarter was $0.78 cents. Adjusted earnings per diluted share was $0.81 cents compared with $0.74 cents in the previous year, an increase of $0.07 cents per share or about 9%. On a GAAP basis, our effective tax rate for the quarter was 22%. We expect the full year tax rate to be approximately 22% to 23% in fiscal 20.

On slide 10, we continue to expand our Adjusted EBITDA margin. For the quarter, our Adjusted EBITDA margin was a record 16.7%, an increase of 100 basis points over last year. We also continue to make progress on driving our ROIC higher, and are now at 11.5%. As a reminder, our Blueprint for Growth strategy goal is to achieve a 19% Adjusted EBITDA margin in fiscal 22, and achieve an Adjusted ROIC in the mid-teens.

Moving to slide 11, net cash from operating activities for the year was a use of $2.2 million, compared to a source of $8.1 million in the prior year. This was related to timing issues. We decided to fund our annual U.S. pension contribution in Q1 in the amount of $7 million whereas last year, we funded this over the year. In addition, we paid out $12 million of annual incentive plan payments in Q1. Regarding CAPEX, our guidance for capital expenditures for fiscal 20 is expected to be approximately $20 million for the year. We still expect our free cash flow to be in the range of $70 to $75 million for fiscal 20.

Turning to slide 12, our total debt was approximately $291 million dollars and our net debt was approximately $235 million at the end of this quarter. Our net debt to net total capitalization is now below 35%. We repaid $10 million of debt in the first quarter and have reduced our term loan debt by nearly $145 million since acquiring STAHL in January of 2017. We made excellent progress de-levering and have achieved a net debt to Adjusted EBITDA ratio of 1.77 times, which is below our targeted net leverage ratio of 2.0 times. From a capital allocation perspective, our plan is to use our free cash flow to continue to de-lever our balance sheet. We expect to repay $65 million of debt in fiscal 20. Please turn to slide 13 and I will turn it back over to Mark.

Mark Morelli: Thanks, Greg.

Let me wrap up by giving you some color around our markets.

We are confident in our strategy and our ability to execute by leveraging the tools in our operating system. We are also seeing increased potential by expanding our target markets through greater traction as a Lifting Specialist and innovating to enable Smart Movement. The result is a better business model, with improved operating leverage.

Despite some of the market weakness, we are also encouraged by growth opportunities we are seeing in specific markets. We see good demand from segments such as Steel, Oil & Gas, aerospace, waste-to-energy, hydropower, defense and government-funded infrastructure. Major utilities and grid system providers are inspecting their power grids and gearing up for the storm season.

The Entertainment segment is growing. We have won some large orders as the touring business is strong and permanent installs are growing. We are expanding our offerings with automation-ready products and incorporating a built-in load sensor for enhanced safety.

Also, our opportunity with automotive looks encouraging. OEMs are investing to compete by designing and building new models of trucks, SUVs and electric vehicles in North America. Model changeover is what drives demand for our products.

While recent industrial market weakness is well reported, we remain confident in our strategy. We expect revenue to be unchanged to slightly improve over last year's second quarter. Adjusted for divestitures and foreign currency translation at current rates, last year's second quarter revenue was approximately $206 million.

We are confident that our Blueprint for Growth strategy will continue to deliver stronger earnings power for the quarter and the fiscal year. Simplification and operational excellence will drive margin expansion and operating leverage.

With that, Doug, would you please open the call for questions?

Operator: [Operator Instructions] Our first question comes from the line of Jon Tanwanteng with CJS Securities.

Jonathan Tanwanteng: Looking at backlogs, they're down slightly year-over-year, what's giving you the confidence in the growth in Q2? And second, can you talk about the quality and mix of orders in the backlog from a margin perspective?

Mark Morelli: Sure. So there's two dynamics that are happening that we talked a little bit about in our Investor Day in June that I can also elaborate on today. The first is a dynamic related to our short cycle business, and this is really the historic Columbus McKinnon business that you might think of. What we see there is some of the folks that we sell to don't want to take as much inventory as they did last year. As a consequence, that short cycle business had dipped and it really hit a bottom in April that moderated in May with some improvement in June and July, mostly in North America. However, we do see the short cycle business in Europe also particularly impacted with the weakness in Europe. However, the total for the short cycle business is trending up, so we're encouraged by that.

The second dynamic that's important to report on is that of our longer cycle project business that is mostly related to the newer acquisitions that we've done over the last couple of years. This is mostly the timing issues related to projects. So we still see the project business as being quite strong in some of the segments that I just spoke about: steel, oil and gas, power. These segments are strong. Projects are good. There are good returns. As a consequence, these projects are continuing to go, and we see very good quoting activity as well. But we do see timing issues related to that business and the timing is what you're seeing in some of the numbers. In particular, what's impacting our timing is the rail business. The rail business has a pretty lumpy impact. So far, we've actually seen some order intake in July for the rail business; about $1.7 million of orders came in July. This is related to orders in Germany, the Czech Republic and China. Hopefully, that describes some of the dynamics we're seeing there.

Jonathan Tanwanteng: Okay. Great. And just a comment on the expected margin of the backlog that you have right now?

Mark Morelli: Greg, do you want to comment on the backlog margins?

Gregory Rustowicz: Sure. So the margins in the backlog are probably going to be a little higher than they would historically be because about $7 million of the reduction in our backlog was in our rail business. But as Mark said, we just picked up some orders here in July. Also, that tends to be a little bit of a lower gross margin than the corporate average, but good operating income because it has lower SG&A.

Jonathan Tanwanteng: Got it. And then you made a nice reduction in your SG&A. You have pretty good guidance for this current quarter. How much more room is there in RSG&A to go down? How much of it is in the 80/20 plan?

Mark Morelli: So I think there are two aspects. Certainly, 80/20 is predominantly hitting the gross margins. But over time, the simplification of our business reduces our operating footprint, and this clearly will have a benefit of our overall spend. So I think what we're giving is responsible guidance for this next quarter and more to come as we make further traction on our simplification processes.

Operator: Our next question comes from the line of Greg Palm with Craig-Hallum Capital Group.

Greg Palm: I guess just following up on the comments on the macro. Taking back on what you said when you reported your fiscal year-end results and Analyst Day shortly thereafter, it seems like you saw the macro slow down a little bit more maybe during that time frame or since that based on the organic growth rate guidance for the September quarter. So I'm just curious, is it more of a one quarter timing around inventory sell in? Or is it just across-the-board? Maybe you can just help us reconcile those items a little bit more.

Mark Morelli: Sure. So let me go back to some of the commentary on the short cycle business. I think in North America, in particular, we saw it really drop a lot in April with some recovery through May. Certainly, we're seeing some upticks in order intakes in July. It's hard to say why that soft patch occurred. It may have been some of the inventory correction issues where folks are a little bit hesitant given the macroeconomic conditions and concerns on tariffs. But we do see that moderating, and we are encouraged by some of the short cycle upticks recently. Whereas in Europe, industrial capacity utilization is off. I think that it feels softer in Europe right now. We hope to offset that with some of the strength that I spoke about in our earnings call and some of our deployment areas of strength. We are definitely seeing areas of strength, so it's important that we work to mine those opportunities and get some of our growth out of that. So we're actually pretty encouraged by what we're seeing, and there is nothing that we're seeing that would indicate it would derail our strategy at all. We're very focused on our strategy. We're very confident that our strategy is right for these kind of market conditions. So I would say, generally speaking, we're pretty encouraged with the visibility that we have.

Greg Palm: Got it. That's helpful. Curious if you have any data or comments on what you think the overall market is growing. It seems like over the past two to four quarters, the market share gains have been accelerating. So just curious to get your thoughts on that. And obviously, what your expectations are going forward as well?

Mark Morelli: Yes. I think we have seen some market share gains over the last two years, some of our initiatives on strengthening the core, some of the deployment in these growth areas. As you can hear from the remarks on this call, we continue to innovate, and I think we're capturing some market segment growth as well. So we are encouraged by what we've been doing and the traction we've been getting.

The overall market, I think there is some data that's written on these. We don't spend a ton of time on what is occurring there because I think what we really focus on is our opportunities to gain share or opportunities to grow. We do know that Konecrane reported on July 25, and they have an industrial equipment market segment that saw orders decline about 3.5% at their constant currency basis. So we feel pretty good about the traction we're getting and the direction we're headed.

Greg Palm: Great. And I guess just last one for me. Greg, I think you had mentioned in the last quarter about the goal or target in terms of operating income growth in the double digits this year versus last. I mean, in the light of a little bit more slowdown in the macro, is that something you still think is achievable or not?

Gregory Rustowicz: Yes. We actually do because, remember, the whole strategy is predicated on internal improvements. We said that we can drive double-digit earnings growth in a low sales growth environment. That's what we're seeing right now.

Greg Palm: Okay. Great. And I guess that would probably inherently imply that gross margins tick up from what they were in Q1 even as maybe the sales level comes down a little bit, is that a right way to think about things?

Gregory Rustowicz: I think, long term, that's the right way to think about it. There are seasonal impacts on our gross margin percentages as you know, but we continue to work hard to improve our factories and our productivity in our factories. We got really good pricing this year so far at 1.8%. We think we have a handle on inflation, and that for the most part has been tamed this year. What we're seeing on that front is really carryover impact from last year. So we would expect for the year to have higher margins than we did a year ago, and we're seeing that now.

Operator: Our next question comes from the line of Walter Liptak with Seaport Global.

Steven Friedberg: This is Steven Friedberg calling in for Walt. So I want to talk about price versus cost. I know you guys mentioned you're positive in Q1. But I was hoping you could provide some color on fiscal 2020 and see how the cadence plays out and if there's any surcharges are rolling off?

Gregory Rustowicz: Sure. So I'll take that one. So for pricing, as I just mentioned, we got about 1.8% price in the quarter that did include some benefit from 80/20, and we would expect that pricing level to essentially hold for the rest of the year. Most of our price increases already have been announced and have been implemented. Our standard price increases have been announced and implemented, and that's done by essentially April 1. So we're pretty confident that pricing is going to be at about this 1.8% level.

Steven Friedberg: Great. And then turning to cash flow. I know it was weak in the quarter. I know you guys commented $12 million for the incentive plan. I guess can you talk about the rationale of prepaying that $12 million as well as the cadence for fiscal 2020?

Gregory Rustowicz: Yes. So let me just clarify something. The $12 million is the annual incentive plan payment, which was actually a larger payment than we've historically had largely because we had such a great year last year. That is always paid in June. So that wasn't the timing issue. The timing issue was really on the U.S. pension plan contributions where we paid $7 million in the first quarter. We chose to do that. We used some of the proceeds from our divestitures a year before. We earmarked that for this payment. So we chose to pay it early. You do get some benefit from it. You get the expected return on asset percentage, which will help EPS a little bit. But it was really our decision from a timing perspective that it made sense for us rather than have the cash sit in the bank.

Steven Friedberg: All right. And the cadence of cash flow throughout the year?

Gregory Rustowicz: That's definitely going to improve because if you think about it, there was $20 million of cash outflows in Q1 that are not going to repeat in Q2, Q3 or Q4. One other point I think is relevant here is that we do expect to pay down $65 million of debt. We paid down $10 million already. So there's at least another $55 million, which will get spread over the next three quarters.

Operator: Our next question comes from the line of Joe Mondillo with Sidoti & Company.

Joseph Mondillo: Just regarding, I guess, Blueprint for Growth, 80/20. Just wanted to make sure I have or understand what your expectations are and cost. You mentioned the $10 million, and that's maintained from prior. And I was under the understanding that about $2 million is going to come from that Chinese facility. But is that more so fiscal '21? And then is there anything else in this bucket of restructuring or improvements that we should expect?

Gregory Rustowicz: In terms of what we expect from 80/20 this year, we're expecting about $10 million of incremental operating income, and that's on top of the $8.5 million that we had last year. So in terms of the consolidations, those are not specifically called out as part of the 80/20, $10 million. So as we mentioned, the Ohio plant closure is already completed. That's going to be $2 million of savings for the year. $500,000 was already achieved in Q1. We talked about that on the call already.

Then for our China consolidation from two into one, that is underway now, and we don't expect it to have a material impact on our operating income this year, but it will be mostly next year because it will take us into our fiscal fourth quarter to have that completed.

Joseph Mondillo: Okay. Perfect. And then SG&A, the $46 million for the second quarter, is any of that lowering from the first quarter related to more rail projects that require less SG&A? Or is that more so related to mostly just you guys, 80/20 and cost reductions, et cetera? And then how should we think about that for the second half of the year?

Gregory Rustowicz: So the $46 million, I would compare it to our run rate in Q1, which was $45.1 million. So as we look at some of the investments that we plan to make in the upcoming quarter, we think it's going to be closer to a $46 million level. We're certainly going to be adding some more on the new product development side of the house, and that's going to be an important driver of growth for us going forward.

For the second half of the year, at this point, we haven't really come up with guidance on it. So it can depend on quite a few things. So I think we should probably just stick with our Q2 guidance at this point.

Joseph Mondillo: Okay. And then, Mark, I wanted to ask about the growth factors that you presented at the Investor Day, R&D, Compass, kit cranes, engineered products, and all those types of things. I know you've probably started to see maybe some benefits, but I would guess that we're in the early stages. Just wondering at what point in time should we anticipate starting to see a benefit from these initiatives?

Mark Morelli: I think you're right. It's early innings for ramping the growth engine, but I think we are beginning to see some of that trickling in now. We're encouraged on variable speed. We're encouraged on what we're seeing from some of our commentary today through some of the operating leverage that we're getting from these new products at higher margins. We're really encouraged by it. So I would think that we should start seeing greater traction as we progress through this fiscal year.

As you know, getting some of the things out through product development can take a bit of time, but I'm making pretty regular updates on our earnings calls, on our launches and some of the progress we're making. I think this is going to be accretive through this fiscal year.

Joseph Mondillo: All right. And then last question, Greg, just on the tax rate. Is 22% a normal tax rate at this point? Or is it still the 25%?

Gregory Rustowicz: So we have lowered where we think our effective tax rate is going to be from the 25% we talked about at the Investor Day to 22% to 23%. We think that with the current mix of earnings we're anticipating, that's a pretty good range of where we expect to be. It is lower. As a March 31 company, we have to do very detailed effective tax rate calculations as of the end of the fiscal year, which has now been completed. So now that we have additional information, we think that 22% to 23% rate is the right rate for this fiscal year.

Operator: [Operator Instructions] There are no further questions in the queue. I'd like to hand the call back to management for closing comments.

Mark Morelli: Great. Thanks, Doug. Thanks for joining us on today's call. We appreciate your interest in Columbus McKinnon. Have a nice day.

Operator: Ladies and gentlemen, this does conclude today's teleconference. Thank you for your participation. You may disconnect your lines at this time, and have a wonderful day.