Worthington Industries_Baird Global Industrial 2021_November 11 2021

Amy Teske: Good morning. I'm Amy Teske from MC Dory's Machinery and Diversified Industrial team here at Baird. I'm pleased to introduce Worthington Industries, which manufactures value add steel and metal products. Joining us today with an update on the company is CFO Joe Hayek. We will start with a formal presentation. We will not have time for a Q&A at the end, given that Worthington is in quiet period right now. With that, I will hand it over to Joe.

Joe Hayek: Thank you, Amy. And good morning, everybody. Thanks for joining us and spending part of your morning to learn more about, or get an update on Worthington. Big thanks to the Baird team for having us. I know we've all gotten used to virtual presentations and so hopefully you get as much as you can out of this. I personally, and hopefully we collectively look forward to being in front of each other at these events sometime in the near future, as soon as conditions permit. But at any rate, we'll jump right in, give you kind of a quick overview of Worthington, talk about some of our value drivers and some of the things that we've been up to. I would also mention that yesterday we had an investor day and went into a great deal of detail on our business segments, on our strategies in those business segments.

Joe Hayek: And so that is posted on our website from start to finish, it's about an hour and a half and you'll hear if you choose to listen in, you'll hear from our CEO, from our chief operating officer and then from our business unit presidents. All four of them, in addition to some financial information from me. So please feel free to take a look and a listen to that if you are interested. Quick update, Safe Harbor, you've all seen this before, but appreciate you looking it over here one more time. And then we'll jump right in. So, Worthington was founded and is still headquartered in Columbus, Ohio, about 66 years ago. Three and a half billion in sales, $604 million in adjusted EBITDA adjusted meaning just not accounting for one time items or structuring gains or losses. That's a TTM number as of the end of August. 53 facilities in seven countries, that number of seven does not include our pending acquisition of Temple Steel, which will bump up that number just a bit.

Joe Hayek: A lot is made of corporate citizenship what I mean, most people think about it as ESG. We think about it as corporate citizenship and sustainability. We've actually been at this for quite a while. I won't read these highlights to you, but one of the most important things that companies like us can do is make sure that everybody that comes to work every day goes home in the same shape that they did or in better shape. We're very proud of our safety record. We can always do better and we have numerous programs in place all over the company to try and make that happen. People are our most

important assets and we take great care to be sure that we are taking care of them and taking care of each other.

Joe Hayek: We recycle 96% of the waste that we generate. We're trying very hard to encourage students, younger people to think about jobs in a manufacturing setting or for a company like ours, we've had some success there. In terms of our community outreach over $2 million in the past year to almost 50 nonprofits that are focused on all kinds of things from increasing diversity in certain areas, to the homeless, to things that people in our company and in our communities really care about. And we're very happy to be able to make at least a small difference in a contribution to those efforts. We published our 2021 Citizenship and Sustainability report in late September. That was our second, that is also available on our website and so if you'd like to take a look at that, I would certainly encourage you to do so.

Joe Hayek: These are all things that we're happy that we're doing. These Green Star Awards and these initiatives are internal awards that we've had in place for over 10 years. And so, as what you see in the public was becoming more prevalent, we've been at this. We know we can do better and we intend to and so you'll see more from us in this regard over the coming months. In June we took what was our pressure cylinder segment and broke it into three segments. Historically, we've had two segments, the steel processing business, and then the pressure cylinder segment. We, as a team had been talking about the way that we think about ourselves and the way that we are focusing our strategies, it made more and more sense to us to stop defining ourselves and stop communicating our strategies based on what we make and made much more sense to us to think about things relative to the end markets that we serve.

Joe Hayek: And so we'll talk a bit more about this, but building products, consumer products and sustainable energy solutions are the three new segments. And as we think about what we're doing, you can see some pictures there. The building products business is your HVAC oriented systems, so that's refrigerants, cylinders, and it also includes foam and adhesive, which are oftentimes used for insulation or for roofing or flooring applications. Includes our water business where we have tankless hot water heaters, expansion tanks, and well expansion tanks for people that are not on the water grid that they are on kind of on a well system, all focused around water in that regard. Building products also contains two of our joint ventures. WAVE, which is the picture you see there on the bottom, which is the grid based on products that are in drop ceilings and acoustical ceilings.

Joe Hayek: That's a 50-50 JV between Worthington and Armstrong Ceilings, AWI. It also includes ClarkDietrich, which is a metal framing company that we own 25% of with our joint venture partner, MISA. The consumer products business, really market leading branded products, outdoor living tools and celebrations. You'll see the Bernzomatic fuel tank and torch there. Lots and lots of applications ranging from professional applications if you're brazing pipe, copper specifically if you're in plumbing applications, but outdoor applications, camping, like the Coleman camping cylinders, that Coleman brand for those cylinders is also our brand. Tools-you'll remember that we acquired a company called General Tools & Instruments early this year in February. Fantastic acquisition for us, garden tools, specialty tools. Not trying to be somebody that wants to compete with

Stanley Black & Decker or anybody else, but smaller niche markets for those tools, really a terrific acquisition for us. Gave us a global supply chain capability that we're really happy with.

Joe Hayek: And ultimately Celebrations. One of our big products is Balloon Time where you are trying to have a party at somebody's house instead of going to the florist or the shop, and you want to do it yourself, you can do that through the Balloon Time products. All of these products typically are going to be found at retailers, Home Depot, Lowe's, Walmart, the specialty stores, et cetera. And then Sustainable Energy Solutions ultimately is a European based business for us, but really focused around Hydrogen, CNG, and adjacent sustainable energy markets as the economy globally, and it's happening much faster in Europe and Asia than it is here in the states. But as they transfer away from diesel fuel to Hydrogen and CNG specifically and we're really well positioned there. We've got lots of products in the market today. We just completed a very significant investment and expansion in our plant in Austria.

Joe Hayek: And we acquired a company in Germany in January of this past year, that really focuses on the solutions part where you can power a bus, or a truck, or a smaller truck, any obviously a car with Hydrogen or CNG. So right now, lots of applications on the CNG side of that for automotive in Europe, but lots and lots of upside related to Hydrogen, specifically for the commercial transportation market. So we're really excited about that. I'll talk more about steel processing, which is our biggest and a very, very great business for us in a couple of pages here, but just wanted to give you a feel for those three new segments where pressure cylinders used to exist for us.

Joe Hayek: When we talk about our sales three and a half billion dollars, the steel processing business which is heavy automotive, you can see that 37% of our revenues goes into automotive, but and its up above and beyond that there are really nice sort of diversity kind of end markets that we're selling into. And we obviously have different ways that we go to market in each of those areas as well. And then you look at our adjusted EBITDA. Steel is having phenomenal success taking share, and with the rising prices of steel in the last year and a half, that's also been a tailwind for them, but you can see the mix of the adjusted EBITDA by segment. Our adjusted EBITDA is, as I mentioned earlier, just over $600 million in the 12 months ended in August.

Joe Hayek: I'll talk about our growth strategies. I mean, we're very self aware and our end markets don't grow all that quickly. They're not going to grow at 10%, they're not going to grow at 15%. We aspire to grow much more rapidly than GDP, which is where lot of the industries that we play in might see as a typical growth rate. Our complimentary value drivers, we've been at this for a while, but we're having a lot of success with each of these. There's transformation, which is our business system. And I won't read the bullets to you, but it's ultimately how do we do better every single day in all of our processes, whether it's on the manufacturing floor, whether it's in a sales application or whether it's in a back office application for finance or on the supply chain. Innovation, not just to say we have a new product, but innovation as a discipline. How do we look at the end markets that we're in? A lot of which haven't seen innovation for decades, and how do we disrupt ourselves?

Joe Hayek: How do we think about other things that our customers really are desiring? Voice of customer is huge for us here. We do a lot of work with voice of customer and ultimately try and use that to discern what our next pipeline addition should be. And then M&A we've spent a lot of kind of time and attention pruning our portfolio over the last couple years. We've also made three acquisitions this year with a fourth that is pending, that I'll talk about. And so we're really pleased that we're able to do better with our base business, take share through operational excellence, but also innovation, and then expand our business through acquisition that is strategic, that has a high cashflow stream associated with it, and possibly some lower asset intensity than our current businesses have. And we're very excited about what that has meant to us over the last couple years, but also think that it positions us really well as we move forward.

Joe Hayek: So I'll go through a quick example of each of these and transformation first. We have to ultimately update these slides sometimes because we have these phenomenal projects and these successes that we celebrate internally, but it's important to refresh them. And so the way that we think about transformation is at this point, the really low hanging fruit for us, we picked several years ago. But as we get more and more intentional about how we do our business, how we think about things. Machine censoring analytics is going to become an increasingly important part of this. So, not a burning platform issue here, but hey, we have downtime in our machines. Every company that does what we do is going to have that. So how do we get better about predictive maintenance and how do we get better at reducing our downtime? Well, we partnered with a startup company and installed remote sensors and a monitoring solution in at first one of our facilities, and now several of our facilities.

Joe Hayek: And as you all know, sensors now are not that expensive. Where the magic is, is how do you understand what the sensor should be measuring to be able to better predict coming downtime, or hey, might want to think about this machine over here. And so how do you dial in these sensors to measure the right things? And then how do you use AI and analytics to then predict what might happen so that you can act in a way that is going to avoid downtime. I'd rather have two hours of downtime rather than 20 hours, two weeks from now, or two days from now. And so avoided a million dollars in lost earnings and 350 hours of unplanned machine downtime. That all by itself isn't going to move the needle for us, but we're doing these things all over the country, not just in this setting, but in all kinds of places.

Joe Hayek: And so for us, this quest to constantly improve is not just for improvement's sake. There are real measurable returns for us that we kind of understand and model before we take on these investments. But we're really happy, not only with the investment, but with our team in analytics and in transformation and all of these things that we're doing, because those investments in people and really setting up our people to be successful is where we're going to make smart investments on the capital side and ultimately be much better off in adding shareholder value as a result. Innovation, same story. We've got lots of things in the pipeline. This is a digital fuel gauge for a portable cylinder. You want to understand whether you need to take two cylinders with you to a tailgate or on a camping trip or wherever it is that you're going. If you're going to be working on a project or a pipe, you might want to understand how much fuel you have.

Joe Hayek: That never been a possibility before. Well, now it is. You can see where you can buy these things. We designed this, we had it manufactured for us because you look at that gauge that the gentleman's holding and you can see that's not our core competency. We don't make those. Other people are better at that. And one of the things that we've really embraced over time is that there are people, we don't need to make everything. We shouldn't make everything. There are people whose expertise it is to do these things. So, let's design them. Let's sell them, but let's have somebody, a partner of ours manufacture them. So, great early returns on this. Again, not going to all by itself, move the needle for us.

Joe Hayek: I think the slide we had on this last six months ago was kind of a smart lid for larger propane tanks using the internet of things. All of these things, taking them together is a much better way to think about what we're doing. Because again, it's not just a project. It's now for us a discipline. So, acquisitions. We have an acquisition that is pending. It was announced last week, forecasted to close in early December. But let's talk about the steel business for a minute. Our steel business is exceptionally unique. We have a very unique way of serving our customers. We buy a lot of steel, more than almost anybody that's not a pure distributor or a big three or north American automotive manufacturer. We have phenomenal pricing groups and purchasing groups so that we can understand what customers need, how we can get them what they need.

Joe Hayek: We've been challenged with the market in the last year with supply chains, with freight, with trucking, with all of the things that have been happening with steel pricing. Our teams are literally world class and it has not been without its challenges, but the way and the markets that we really show our customers and ourselves that we're exceptional. We can always be better but that we're exceptional in markets like this that are challenging. And so one of the things that we've been doing within our steel processing business is to trying to position ourselves, to get into end markets that are going to grow more rapidly than our traditional markets. And ultimately that has led us to lightweighting and the coming electrification of vehicles and the electrification of transportation and a lot of the things that are associated with that. You saw us acquire assets from the former Shiloh earlier this year, again, that's big in terms of lightweighting and trying to fuse aluminum and steel together.

Joe Hayek: But we announced last week that we are acquiring Temple Steel, a global leader in the electrical steel market. And so for those that aren't familiar with electrical steel, it is necessary for all electric motors. And since whether that motor is powering something that you see in your house or in a car or in a transformer that you see kind of powering the grid or moving, that the transmission of electricity from place to place to place. Electrical steel, there aren't that many sources of it globally. There are more and more that are coming online as people understand what's happening globally, but what Temple does is ultimately take that steel and stamp it and make it into a very usable piece of those motors. We're very excited about it. And I'll give you a bit more detail on some of those markets, but you can see the specifics here, $255 million plus assuming certain liabilities. And then you can see their revenue and adjusted EBITDA, excluding some inventory holding gains that they've had.

Joe Hayek: Really excited about this acquisition and what it means for us and kind of how we will be able to partner with the Temple team to make their business even better and bigger and more valuable than it was. So specifically there are what I'll call the three mega trends that are really happening with respect to transitioning away from diesel or other fuels to renewables. Electric vehicles is a big one. We mentioned early on Temple is a great set of solutions and a great set of customers. Automotive is going to be a massive growth industry for electrical steel. Guess what we're really good at is understanding the supply chain and automotive selling into the OEMs and making sure that everybody is happy with the solutions and the timeliness that we're providing. Great, great match there for Temple and for Worthington. Reducing the carbon footprint and then the aging infrastructure worldwide as you think about things, another big market. They're probably the biggest market for Temple as we're thinking about a lot of things is the transformer market and the transmission market.

Joe Hayek: Bottom line, as people use electricity for more than they have historically that they're substituting electricity for something else. And as the sources of electricity generation move from traditional power plants to wind or solar or other things, right? Things have to be transformed, right? They to be moved, electricity has to be moved from where it's generated to where it's ultimately used. And so you need new infrastructure, but you also have aging infrastructure. So you not only need new transmission lines, but you need to replace aging transmission lines all over the globe. That is going to put companies like Temple, who again, is one of the global leaders today, in a really good spot in terms of potential growth.

Joe Hayek: And I talked about a lot of this, but if you just see, look at the estimated CAGRs, and these are McKinsey's numbers for the next sort of four years. Some of these things I personally believe specifically with the transformers, that that number is going to accelerate, just because I personally think that it has to maybe not before 2025, but then beyond, as you really start to get to the higher slope of the hockey stick of the growth rate of all these different things. So a lot of these slides, I will also tell you are on our website. Now they went up just post acquisition. And so I'm going through them pretty quickly here. We'll actually go to the next one, just because you can in fact see these. So, global footprint from Temple, Canada, the United States and Mexico, but lots of presence in terms of the marketing and sales side in Europe, but then also manufacturing in both China and India.

Joe Hayek: And so really well positioned globally to serve these markets that we've just talked about because there'll be different growth rates and different starting places. But I think everybody is pretty convinced right now what's going to happen. And we feel really good about this partnership as we go forward. Not a lot that we can say ultimately until the transaction is closed and until we get into it but we have a lot to learn. We think we'll have a lot to offer the Temple team and we're really excited about what we'll be able to do together. So a couple more slides from me. Our financial goals, this is a slide that we've gone over before, but we absolutely want to, as a company through M&A, and organically increase our margins and decrease our asset intensity. We intend to continue to do things that reduce our earnings volatility.

Joe Hayek: We understand that we're a cyclical company. If you look at the profiles of steel prices, and then you look at our downstream businesses, specifically consumer products and building products, we're on our way to doing that. We are an investment grade credit. We have modest leverage and ample liquidity. We intend to continue following that path. Along with that goes our approach to capital allocation, which so it's an overused term, but I would always refer to as very balanced and I'll get into that in the next slide. But then that last piece is, we'll call it the rigorous capital discipline. We have in the last couple of years gotten smaller to get better. We have divested of several non-core or non-profitable businesses or locations. That's freed up capital, but it's also freed up human capital and so that we can focus on our existing businesses and adding strategically to our businesses through acquisitions or JVs or any other transactions. And we're really happy about where we are and with what we have in front of us.

Joe Hayek: We talked about balance capital allocation. I won't read these bullets to you, but including the capital deployment, assuming the Temple acquisition closes in the next month or so in the last 10 years, we will have spent roughly $2 billion on acquisitions and CapEx. And we will have spent roughly a billion and a half dollars on share repurchases and dividends. So, we like to measure ourselves not on a quarter by quarter or year by year basis, but over the course of time. We have decreased our share account by 30% over the last 10 years. Our dividend yield is right around 2% and so we're happy with our ability to return capital to shareholders and also invest and grow our business. And we'll continue to do that. Our liquidity profile, we don't have maturity until 2024. We ended Q1 with a fair amount of cash, and we have a $500 million revolver that's available to us, that is undrawn. And even though we have been investing, I'd call it in working capital we've added $322 million to working capital in the last nine months.

Joe Hayek: That's a reflection of rising steel prices. If, when, as steel prices come down, that cash will come back to us, which will provide us yet another source of liquidity. Now you can see here, the consolidated financial results, again, this performance due to excellent performance and some market tailwinds in the steel business, but also the historically more profitable, but smaller businesses in building products, consumer products, and sustainable energy solutions. And then I'll close with our investment highlights and not to read through them again. But we feel like we're in end markets that are really attractive for the next five to 10 years as people have refocused their time spent around the house, our consumer facing and building products businesses will continue to benefit as we look at the future for transportation and for the way that things are powered globally in the electrical steel space, but just in our steel space broadly.

Joe Hayek: We have an excellent, excellent market share position because of the way that we've been doing things for decades. And so we're going to leverage that position to continue to take share in markets that we know well and are happy with. Balanced approach to capital allocation and certainly our cashflow ample liquidity give us lots of really good feelings, and we're really bullish on what we'll be able to do, as we reflect on what we've done in the last 10 or 15 years, and really focus on the next step. Amy, that is it for our prepared remarks.

Amy Teske: Great. Thank you. We are at the top of our time block, so thank you so much to Joe for participating in the conference today. Our next set of presentations are Advanced

Drainage Systems, LCI Industries, Masonite international for technologies in [inaudible] products. Thank you everyone for attending the Baird conference and have a good day.

Joe Hayek: Thank you.