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NCS - Q1 2018 NCI Building Systems Inc Earnings Call

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PRESENTATION

Operator

Greetings, and welcome to the NCI Building Systems First Quarter 2018 Earnings Call. (Operator Instructions) As a reminder, this conference is being recorded. It is now my pleasure to introduce your host, Ms. Darcey Matthews, Vice President of Investor Relations for NCI Building Systems. Thank you. You may begin.

K. Darcey Matthews - *NCI Building Systems, Inc. - VP of IR*

Good morning, and thank you for your interest in NCI Building Systems. Joining me today for the call are Don Riley, our CEO; and Mark Johnson, our CFO.

Please be reminded that comments regarding the company's results and the projections may include forward-looking statements that are subject to risks and uncertainties. These risks are described in detail in the company's SEC filings, earnings release and supplemental slide presentation. The company's actual results may differ materially from the anticipated performance or results expressed or implied by these forward-looking statements. In addition, management will refer to certain non-GAAP financial measures. You will find the reconciliation of these non-GAAP financial measures and other related information in the earnings release and supplemental deck located on our website.

Our first quarter 2018 earnings were released last night. A copy of both the release and our supporting supplemental presentation can be found in the Investors section of our website.

This morning, Don will make a few comments about the quarter, and then turn the call over to Mark for more specific financial commentary before we open up the call for your questions.

And now, I'd like to turn the call over to Don.

Donald R. Riley - *NCI Building Systems, Inc. - President, CEO & Director*

Thanks, Darcey. Good morning, everyone. Thank you for joining us today to review our 2018 first quarter results.

We are pleased to announce a very strong performance in Q1 by the NCI team. On a year-over-year basis, NCI revenues and adjusted EBITDA were up 8% and 26%, respectively. Gross margins were up 40 basis points. EBITDA grew double digits for IMP, Engineered Buildings and Components.

In IMP, external sales grew 18%. This strong performance by the team positions us well for Q2, and we continue to be very optimistic about the full year.

As we stated last quarter, we continue to expect low-rise nonresidential construction starts will continue to grow mid-single digits, with the addressable markets for our legacy businesses growing 2% to 4%. IMP, based upon increasing market penetration, should continue to grow at low double-digit rates. Our current backlog in incoming order rates for Buildings and IMP continue to support these base assumptions.

At NCI, our strategy is to leverage our advantage legacy platform to drive higher than market growth rates through expanded envelope solutions for our customers. This is what we refer to as adjacency. The concept of adjacency is an important part of our future growth and is based on our ability to pull adjacent and complementary products through the advantaged sales platform that our legacy distribution channels have created. This model continues to perform well with the Buildings backlog for IMP being up greater than 26% year-over-year.

We recognize NCI and our customers are headed into an interesting period with rising interest rates, expanding inflation and potential trade and tariff complexities, all on top of a growing economy. In this environment, the NCI team remains focused on managing our costs, driving operating efficiency, ensuring commercial discipline and enhancing the penetration of IMP in the marketplace. Based upon these areas of focus, we are in a better position today to deal with any foreseeable volatility than we have been at any point in our history. We have dealt with these periods before and are confident in our ability to manage through them and that 2018 will be a far better year than 2017 for NCI.

As I mentioned on our last call, the 3 key areas of our longer-term strategy are; first, the implementation of advanced manufacturing, where investments in automation and process innovation will further drive down our operating costs, improve margins, quality in service and enhance our long-term operational flexibility. A key element of this initiative is the implementation of an automated frame line for the Buildings business. We are well on our way to having this line operating by Q3. It is on schedule, on budget, with the equipment on site being installed as we speak. This is an incredibly exciting and our largest investment to date in automation. Second, continuous improvement, where we will take advantage of the great work that has been done in manufacturing and delivering further cost reductions with Lean and Six Sigma initiatives across our entire business, further reducing operational back-office costs and simplifying the business. So far, we are ahead of our savings plan for 2018, have trained over 200 employees, have tripled the number of continuous improvement projects being worked on compared to 2017 and are well on our way of building a culture of continuous improvement. The entire NCI organization is getting behind us in an amazing way. Third, NCI solutions, our growth strategy around insulated metal panels and our ability to drive adjacent products across the engines of our legacy distribution channels. Simply stated, IMP grew 18% year-over-year in Q1. I am really pleased with what the legacy and IMP teams are doing on this front. The impact of these elements by 2020 will be $40 million to $50 million, building margin expansion, ESG&A reduction and EBITDA expansion. We are definitely on our way. The NCI team continues to be excited about the potential for our company. We are confident that 2018 will be a better year than 2017, believe we are off to a good start and are excited about what the future holds for us. Our overriding objective remains: establish a business platform that enables NCI to outperform our addressable market within the low-rise nonresidential market while [out expansion] of our operating margins. We now have a more efficient cost structure, demonstrated success in leveraging IMP sales through the Components and Buildings groups and the ongoing implementation of the proven concept of product adjacency. Combined with the rising demand for key products, these strategic actions will prepare us for long-term growth in 2018 and beyond.

I look forward to answering your questions at the end of the call, and I will now turn the call over to Mark for a review of our first quarter financial results and second quarter guidance.

Mark E. Johnson - *NCI Building Systems, Inc. - Executive VP, CFO & Treasurer*

Thank you, Don.

Before I begin, I would like to note that I will be discussing our financial results within the context of our recent business re-segmentation, which we outlined in a conference call last week. As a reminder, in this new reporting arrangement, we now are segregating our insulated metal panel operations into its own distinct business segment. The IMP business had formerly been part of our Components segment. This new segment is composed of the IMP operations of CENTRIA and Metl-Span and CENTRIA's coil coating operations will now be reported as part of our Coil Coating segment.

Turning now to our financial results for the quarter. Our consolidated revenues were up 7.6% year-over-year to $421.3 million as a result of gains in both pricing and volume. Commercial discipline was the more substantial driver this quarter, with the bulk of the gains coming from the IMP business. Although our Buildings and Components segment contributed solid gains as well. The Coatings segment was flat as we have been actively pairing lower margin accounts as we integrate the CENTRIA coil coating operations, which had previously been reported in the Components segment to better utilize our capacity and ultimately optimize our consolidated margin performance in this segment.

In terms of product volume, the gains primarily came from the Components and IMP segments. The Components business posted strong volume gains across product portfolio, with the strongest growth in light commercial end uses and mini storage structures, including roll-up doors. Insulated metal panel volumes were strong but most of the year-over-year growth was in the midrange industrial panels, so the average margin mix was weighted less favorably than the prior year.

Gross margins were within our guidance and up year-over-year, both in terms of percentage and absolute dollars. At 21.8%, they were toward the lower end of our guidance due to less favorable product mix, particularly in insulated metal panels. Elevated transportation costs and weaker performance in the CENTRIA coil coating operations, which I mentioned a moment ago, is being consolidated with our coil coating segment.

From an adjusted operating margin perspective, the increase in our gross margin and our focus on the restructuring and consolidation of our ESG&A expenses enabled a 140 basis point expansion, with roughly 3/4 of the improvement coming from ESG&A reductions. These reductions are part of our previously announced targeted overall cost and efficiency improvement of $40 million to $50 million by 2020, with most of the benefits weighted to 2019 and 2020.

Let me now discuss some items on our balance sheet and cash flow statement before turning to our outlook. As you know, a few weeks ago we closed on a new $415 million term loan as well as a new $150 million ABL facility. Using the proceeds of the new term loan, we retired our 8.25% senior notes and refinanced our $144 million senior secured term loan. As a result, our capital structure has improved markedly and our financial flexibility has greatly enhanced. The end result of these transactions is a meaningful reduction in our debt service cost as our effective cash interest rate will fall from 7% to approximately 3.6% based on current LIBOR rates, which equates to an annual interest expense savings of about $12.5 million. From a working capital perspective, our average metrics for inventory and receivables improved by slightly less than 1 day as compared to the same period in the prior year. Overall, during fiscal 2018, we anticipate generating meaningful operating cash flow enhanced by the reduced interest cost and lower effective tax rates. We do expect that in the near term, increases in raw material costs will likely require the use of working capital as both purchases and sales transaction values increase accordingly and as we prepare for the seasonally stronger period during the second half of our fiscal year. During the quarter, in aggregate, we used $47 million to repurchase approximately 2.7 million shares. This follows the $41.2 million spent in fiscal 2017 to acquire 2.8 million shares.

Turning now to our outlook. Consolidated backlog is up 8.1% year-over-year to $570 million. As Don mentioned, based on our leading indicators, we continue to expect our legacy business to track in the range of 2% to 4% volume growth for the addressable portion of low-rise starts for fiscal 2018. And for our IMP product lines, they should continue to grow at low double-digit rates, thanks to greater market penetration and the ongoing benefit of our intercompany sales of these products. Capital expenditures, which were 1.2% of revenues in 2017 and have typically averaged around 1.5% to 2% of revenues, are expected to be higher in 2018 to fund the initiatives Don mentioned earlier for advanced manufacturing and process improvements and for the carryover of projects from 2017. Capital expenditures are anticipated to be in the range of $45 million to $55 million for the year and be funded from operating cash flow. Of this amount, almost half represents growth or productivity investments. We generally expect the growth and productivity investments included in our plan will provide minimum returns of 25% or more, and we are prioritizing projects with short payback periods. We often see variations between the seasonally slower first and second quarter, driven by inclement weather and product mix changes. It is for this reason that we often find it helpful to consider the first 2 quarters taken together to form the first half. There is a strong seasonal component to our business and the second half is generally the strongest period for construction, driving volume, plant utilization and earnings during that period. We expect to see continued increases in some of our primary input costs as a result of inflation and the administration's recent trade announcements. We have seen similar events before in 2002, 2004 and 2008, and achieved year-over-year growth in earnings and stable or improving gross margins in each of those years. Our internal economic indicators and year-over-year growth in both bookings and backlog are tracking to our expectations and support our continued favorable outlook for fiscal 2018. With these considerations in mind, we currently estimate consolidated revenue for the second quarter will range between $430 million and $450 million, with adjusted EBITDA ranging between

$29 million and $39 million. As a reminder, we have provided additional guidance for the second quarter in the supplemental presentation posted on our website.

And now we'll open the call for your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Our first question comes from the line of Matthew Bouley with Barclays.

Matthew Adrien Bouley - *Barclays Bank PLC, Research Division - Research Analyst*

I wanted to start out with a question on gross margins. Looking at the bridge for the second quarter guide, you've called out mix and transportation costs here and an assumption of higher steel costs. So I guess between those, what's embedded in the second quarter guidance? And really, looking into the second half, what kind of offsets can we expect to see from some of these areas you called out, such as automation and other initiatives?

Donald R. Riley - *NCI Building Systems, Inc. - President, CEO & Director*

Yes. I'll take the first pass of that, and then pass it on to Mark. At the highest level, when we are giving our Q2 guidance, one of the things that we're thoughtful about is -- and in Q4 of '16 and Q1 of '17, we had a lot of pent-up demand for architectural insulated metal panels that pushed into Q2 of '17. And that drove about 250 basis points above our norm for that period due to that mix. And we see that mix normalizing, which is one of the things you see happening in our Q2 for this year. So we do anticipate sequential improvement in gross margins across-the-board for our business lines. And Mark, would you like to give more color to that?

Mark E. Johnson - *NCI Building Systems, Inc. - Executive VP, CFO & Treasurer*

Sure. The transportation cost we mentioned in our release was more related to the first quarter than the second quarter. We do see that dissipating some in the second quarter, not so much because the costs are coming down. They're continuing to be elevated. But because we pass those on to our commercial arrangements. With respect to the automation's impact, we expect to start to see the automated line come on in the third quarter. So we probably don't see too much impact until maybe a little bit in the fourth quarter, but really, that's more of a 2019 opportunity. I would also just comment that in the first 2 quarters of the year, which are very seasonal in nature, they are susceptible to volatility between the 2 periods. We often see Q1 and Q2 vacillate in terms of margins, and that's driven by things like weather and its impact on product mix that can shift during certain weather environments. So it's not unusual to see that kind of variation in a given period.

Matthew Adrien Bouley - *Barclays Bank PLC, Research Division - Research Analyst*

Okay. Thanks for all that detail. The second question, I guess, just on the broader steel market, given all the rhetoric out there. You called out seeing similar events in the past around this. So I guess, what are you doing today to kind of mitigate potential inflation on the pricing and commercial side? And what do you anticipate the reaction is from your customers, if, in fact, we do see more significant inflation?

Donald R. Riley - *NCI Building Systems, Inc. - President, CEO & Director*

Sure. That's a great question. The key is we've been here before, and even with the potential tariffs that are being speculated, and that is the key at this point there, it is all speculation. But we feel good about where we're at in the year. We have better processes and commercial discipline than before in -- across-the-board within our organization and we have great initiatives in place that we're really excited about. And we've been very aggressive and proactive on this front. We're into probably our third price increase over the last few months. And as you know, even before we got into the discussion around tariffs, we knew we were already dealing with an environment of expanding inflation around steel and foam and paint and transportation and labor because of the great economic growth that was going on. And so we've been constantly communicating with our customers. And that's the most important thing to them is helping them understand, helping them stay ahead of it when they are quoting and bidding. And candidly, it's easier to pass through and work with the customers when it's something like this that's highly visible and everybody has access to the same information and can see those costs coming through. The market has been very cognizant of the tariff discussion, the transportation discussion, labor discussions, steel and foam. So that definitely helps us when the customers see and hear it. At this point, when you talk about the impact, steel products continue to remain advantaged, CPI-wise, and Mark can speak to that in a moment, against things like concrete block and precast; more still the optimal solution for structural buildings. The price per ton for buildings has been higher. The average cost for a building could go up anywhere from $5,000 to $10,000 on an $85,000 building is our current estimates. But we are in a growing economy. We have gone through this in '02, '04 and '08, and we feel that we're positioned very well to work with our customer base, to work through that and continue the support of the marketplace.

Operator

Our next question comes from the line of Lee Jagoda with CJS Securities.

Lee M. Jagoda - *CJS Securities, Inc. - Senior MD & Analyst*

So starting with the Buildings' external volumes down about 3%. You managed to hold margins even with a rising steel price environment, which is a nice positive. Can you -- and you highlight commercial discipline as one of the reasons why you've been able to do that. Can you talk about the competitive environment? Are other competitors -- have shown the same commercial discipline? Or -- and if not, how are you combating that?

Donald R. Riley - *NCI Building Systems, Inc. - President, CEO & Director*

So our perspective is, across all of our business lines, we have been very focused on commercial discipline, being candid with our customers about the input costs and pushing that through the marketplace in an effective manner and overcommunicating that. We believe that in general, the competitive environment has been such that they are also demonstrating commercial discipline across-the-board. They recognize and see the same input costs we do and therefore, are having to act on it. Each business acts on it at a different timing and pace based on how they see their costs and their flows in the timing. But we are definitely being very aggressive and not necessarily waiting for their lead. We are focused on leading the way.

Lee M. Jagoda - *CJS Securities, Inc. - Senior MD & Analyst*

Okay. And then just 2 more, if I can sneak them in. One is around the -- can you speak to the tonnage growth in your backlog versus the revenue growth, given the changes in steel prices? And then the other that I'll piggyback on is the CENTRIA coil coating piece. You speak to some inefficiencies as you integrate that. Can you speak to sort of the margin quantification hit in the quarter, and when will we see that returning back to more normal?

Mark E. Johnson - *NCI Building Systems, Inc. - Executive VP, CFO & Treasurer*

Sure. First, with respect to the backlog, the pricing increases definitely outweigh the volume increases. I would estimate the volume inside our backlog to be up in the mid-single digits, low to mid-single digits. And it's important to note, too, that it's often not the case, that all of the backlog is repriced at the same time. So as some of the older jobs come closer to their actual distribution day, they will tend to get repriced at that point in time as well. So I expect to see that continue. On the insulated metal panel front, we talked a little bit about the significant fluctuation in mix that occurred during last year's second quarter. Outside of that, we kind of like the mix that we currently have with the insulated metal panel business and would expect to see that continue for the rest of the year. I do note that in the second half of the year, across all of our businesses, we have significantly more operating leverage during that time and the margins are higher as a result.

Operator

Our next question comes from the line of Matt McCall with Seaport Global Securities.

Matthew Schon McCall - *Seaport Global Securities LLC, Research Division - MD and Furnishings & Senior Analyst*

So maybe following up on a previous -- I don't know if I heard the quantification, but when you look at the Q2 guide, is there -- and I'm sorry if I missed it in the presentation, is there some steel price cost pressure baked into that guidance? If so, how much? And how long would you expect it to persist?

Mark E. Johnson - *NCI Building Systems, Inc. - Executive VP, CFO & Treasurer*

There is some natural increase in the steel prices that is baked into the second quarter and our ability to pass that on and hold dollars to our customers. But the real predominant driver in the margin versus the prior year margin is the change in the mix in the insulated metal panel business. If you look at it sequentially, we are guiding to, at the midpoint, margins being higher in the second quarter than they are in the first quarter.

Donald R. Riley - *NCI Building Systems, Inc. - President, CEO & Director*

We see margins improving across from first quarter, second quarter across each business line.

Matthew Schon McCall - *Seaport Global Securities LLC, Research Division - MD and Furnishings & Senior Analyst*

Okay. So more mix than price cost?

Mark E. Johnson - *NCI Building Systems, Inc. - Executive VP, CFO & Treasurer*

Yes.

Donald R. Riley - *NCI Building Systems, Inc. - President, CEO & Director*

Yes.

Matthew Schon McCall - *Seaport Global Securities LLC, Research Division - MD and Furnishings & Senior Analyst*

Okay. Maybe with the new segment breakdown, can you give us your updated thoughts on the incremental margin targets by segment?

Mark E. Johnson - *NCI Building Systems, Inc. - Executive VP, CFO & Treasurer*

Sure. Give me one moment. As I'm looking for my notes on this, the highest incremental margin business we have is our insulated metal panel business. And that is followed by our Buildings business, and then followed by our Components business, and then Coatings is last. With respect to the margin range, I would say that the total incremental margin across the 3 different product types that are included in insulated metal panels ranges anywhere from 30% to 45%. Within the Buildings business, it's in the 25% to 30% range, within the Components business, it's in the 20-ish to 25% range and then within the coil coating, it's in that 15% to 20% range.

Matthew Schon McCall - *Seaport Global Securities LLC, Research Division - MD and Furnishings & Senior Analyst*

Okay. And then Mark, that's without -- that's just the core leverage on growth. That doesn't include the benefit of some of the savings that you quantify, correct?

Mark E. Johnson - *NCI Building Systems, Inc. - Executive VP, CFO & Treasurer*

That's correct. That's our historical margin, incremental margin.

Matthew Schon McCall - *Seaport Global Securities LLC, Research Division - MD and Furnishings & Senior Analyst*

Okay. And just curious. I'm not sure why it wasn't in there, but volume for IMP, that wasn't included. Is there a reason you won't include that or didn't include that?

Mark E. Johnson - *NCI Building Systems, Inc. - Executive VP, CFO & Treasurer*

The measure we use for volume across our legacy businesses has historically been tonnage. And that has to do with the predominance of steel through the product line. But with the insulated metal panel line, that is not a real measure of the activity level because of the varying thicknesses of panels, and so on. So we don't have a good volume measure that answers more questions than it asks.

Matthew Schon McCall - *Seaport Global Securities LLC, Research Division - MD and Furnishings & Senior Analyst*

Okay. That makes sense. And then, maybe a bigger picture question for you, Don. The potential benefit, I think we've talked about this in the past, just wanted your updated thoughts. The potential benefit from your business, maybe from a customer perspective, from tax reform versus the opportunity that could come from any regulatory changes, specific bank regulation changes, any update there? I mean, the growth rates you're talking about are nice, but any kicker that you expect from tax reform? Any kicker that you expect from some regulatory changes or that you're hearing about from your customers?

Donald R. Riley - *NCI Building Systems, Inc. - President, CEO & Director*

Sure. Clearly, both of those fronts ultimately will be positive. We'd love to see regulatory reform, the banking reform will be great and the tax reform has already gotten through. All of our customers are incredibly optimistic about it. What we generally hear and what we would expect is it will take probably 6 to 12 months before you'll really start seeing the impact of those capital investments to start flowing through. They'll see what the bottom line impact is, how it's affecting the cash flow, they'll then start sending their plans, and so we would anticipate it would be either late this year or early next year before we really start seeing the impact of that and -- of those investments and that's the sentiment coming from our customers. So fundamentally, they're saying, they're excited, they see a lot of potential but they don't anticipate in the short term that we're going to see a bump, but they do anticipate in the long term, we would see something come out of that.

Operator

Our next question comes from the line of Steven Fisher with UBS.

Steven Fisher - *UBS Investment Bank, Research Division - Executive Director and Senior Analyst*

You guys have talked about in the past the natural hedge that you have in the business on steel prices. Can you just talk about how that played out in the quarter within the segments? And how you see that playing out in Q2 within the segments?

Mark E. Johnson - *NCI Building Systems, Inc. - Executive VP, CFO & Treasurer*

Sure. The natural hedge basically comes from the fact that our business segments have varying lengths of cycles. So some are very quick. They'll take an order today, they'll be delivering it next week, and some take longer. And so the longer cycles, like the Buildings group, may take up to 90 to 120 days to actually begin to manufacture a product for a customer. So there's a longer period of time for steel variation to impact the profitability of that order. Now none of our orders are committed in terms of -- we can change the price, particularly if steel prices change. We have the right to do that under our contract and we do that quite regularly. As prices are increasing, we tend to see the Buildings group margins compress as they're chasing that cost up. And -- but on the flip side of that, we tend to see margins expand in both the Coaters and Components business because they're very quick turn. We really didn't have too much noise this quarter from either event because we've been very focused on the commercial discipline across the group and we have all of our divisions passing along the steel costs and other input costs at the rate we want them to pass it on. So it was not a significant driver to this quarter.

Donald R. Riley - *NCI Building Systems, Inc. - President, CEO & Director*

I would say, similarly, we don't anticipate that being a material factor in Q2.

Mark E. Johnson - *NCI Building Systems, Inc. - Executive VP, CFO & Treasurer*

I agree. We've seen some pretty volatile steel cost events in the past. 2002 was a really good example, where there were 30% tariffs implemented during that year. And it caused quite -- some reaction in the steel costs. It was something that had not been seen before in that area. And in that time, with very drastic increases in steel, I believe it went up, on average, 18% that year. But it spiked at one point as high as 48% higher. And during that time, our margins held the same as they were in the prior year and our earnings went up. So we've managed through this several times, 2002, 2004 and 2008. In all of those cases, our margins for the year were flat or better than they were the year before. We're often asked what the impact on volume is during environments like that. And while we have not seen a notable demand element from that, we do note that during the points of extreme spiking, where there begins to become questions about will the price begin to decrease, we do see customers accelerate before the price increases, and then try to decelerate as they wait to see if the prices are going to decrease. But outside of that noise, that plays out over a quarter or 2, we've not really experienced a demand impact from that.

Steven Fisher - *UBS Investment Bank, Research Division - Executive Director and Senior Analyst*

So that's helpful. Is the point here on the discipline and the lack of margin impact, is that you're finding the ability to pass everything along more real-time compared to how it played out in the past?

Mark E. Johnson - *NCI Building Systems, Inc. - Executive VP, CFO & Treasurer*

Yes. We are attempting to change what would have been a more challenging period for our Buildings group so that it's not so challenging. And at the same time, retain advantages in the other parts of our business where we can.

Donald R. Riley - *NCI Building Systems, Inc. - President, CEO & Director*

This has become a critical -- has been a critical area of focus for us is how well -- and coaching the teams on how well they manage through these periods and manage the steel and manage the margin and not just recovering the cost but ensuring we're making the margin on these opportunities. Mark and his team has done a great job on helping the teams with that.

Steven Fisher - *UBS Investment Bank, Research Division - Executive Director and Senior Analyst*

Okay. Great. And then, just you noted the margin mix in IMP. Is there any particular broader trend that you discern here? Or was that just a temporary factor in the market?

Donald R. Riley - *NCI Building Systems, Inc. - President, CEO & Director*

It was more a temporary factor in the prior year. And as Mark noted, we're comfortable with where the mix is at for 2018, and we're really excited about the growth they're showing and the backlog that is in both IMP and Buildings for that business. So the penetration of that product continues, the value proposition for that product continues and we continue to invest in that as a core part of our strategy for the company.

Operator

(Operator Instructions) Our next question comes from the line of Scott Schrier with Citi.

Scott Evan Schrier - *Citigroup Inc, Research Division - Senior Associate*

I wanted to follow up, Don, on those remarks on IMP. Can you talk a little bit about what you're seeing in the market that enables this strong rate? Are customers generally receptive to the product? Is it gaining more acceptance and becoming easier to sell?

Donald R. Riley - *NCI Building Systems, Inc. - President, CEO & Director*

Sure. No, that's a great question. And I noted, we've seen 18% year-over-year growth in Q1. I think we commented that the Buildings backlog end of Q1 was up 26% inside of their backlog. As we've talked about in the past, the gain for IMP is around wall systems penetration. In the U.S., we believe insulated metal panel penetration is 3% to 5%. Europe is closer to 12% to 15%. And we see key things, as we've talked about before, accelerating that growth from the 3% to 5%, closer to the European levels. And the key factors in that are performance and durability, so these panels have a longer life, minimal maintenance and they're light and strong and they also have superior air, vapor water and thermal barriers. And then, they're more energy efficient compared to alternatives, so as we've talked about, as energy codes become more stringent, these solutions become more effective compared to their alternatives. And then, ease of installation. So as you see labor costs continue to escalate, it continues to advantage these solutions because it saves time and money on the job site where you're click and play and you're replacing -- you have 1 step that replaces 3 or 4 steps in multiple trades, so your labor costs and time on the job site is lower, your coordination costs are lower, ease of installation is lower. Then the other key thing with these is that there's a lot more design flexibility, which architects and owners like. So you put all those factors together and you have the accelerant of the energy codes and labor and it just helps this penetration. And so the key in the marketplace is educating everyone on these value propositions to drive that increasing wall penetration. That's why you hear me talk about -- the real competition isn't the fight over the 3% to 5%, it's the fight to get to that 10% to 12% penetration, because every 1% is about $160 million to $180 million in incremental market for IMP.

Scott Evan Schrier - *Citigroup Inc, Research Division - Senior Associate*

And then, given the attractiveness of the business, can you talk about the competitive landscape? I mean, it's a high margin business. Are there other competitors that are coming to this market? Or is your product offering and your knowledge able to kind of keep control of the market, so to speak?

Donald R. Riley - *NCI Building Systems, Inc. - President, CEO & Director*

Well, as we shared, there's 1 primary competitor in Kingspan and they are a great competitor, global company. And the way we look at the marketplace is, one, the battle is not against insulated metal panels but it's against wall systems. And so how do we educate, specify and sustain that growth on that front? I'm sure that other people look at our growth and listen to what we're talking about and say, "All right, what would it take to get into insulated metal panels in the U.S.?" You have the top 2 players that have greater than 90% share. In order to be successful in the marketplace, you are shipping a lot of air, so you need a footprint across the U.S., a plant which investment is feasible for companies, is around $15 million plus the land that you have put it on. That's an investment people can make. But it would take you approximately 18 months to greenfield that plant. You then have to go through the process of learning how to manage the foam systems because there's both art and science in the foam systems and making them effective. And then, you additionally have to get, for each line you have, those foam systems and products certified in the marketplace for all the codes you're trying to have them compliant with, of which includes physical testing. So if someone wanted to come in and try and do this from the ground up, it's possible but it would take them a fair amount of time to accomplish that. And in that period of time, our focus is in our product competitive positioning and increasing the share and materially growing the size of the pie that we have available.

Scott Evan Schrier - *Citigroup Inc, Research Division - Senior Associate*

Great. And then, one more for me on the bidding environment, more so in Buildings. Can you talk about what you're seeing in terms of project complexity and size and how that translates into your backlog visibility in the segment?

Donald R. Riley - *NCI Building Systems, Inc. - President, CEO & Director*

Sure. So I will say that the feedback we are getting from the Buildings group and what they are seeing is, that we have started to see a steadier increase of the mid- to larger sized projects for us. And that's been pretty exciting for them, so that pace has picked up probably in the last 3 to 6 months. Additionally, we had been seeing in our backlog a fair amount of work that had been coming through as permit and approval, where we would prefer to see that more as ready for production and for shipment. That trend has started to change, which we would expect with seasonality. So we're starting to see that mix back towards production starting to come through. So that is also positive. Their builder network appears to be upbeat across-the-board. They are seeing a lot more quoting activity across-the-board. And our backlog has been showing very positive signs and has been building over the last few months. So we see all those trends as very favorable. And ultimately, we see it supporting our view, readily, of low-rise nonres addressable for us for the year, being 2% to 4% and IMP growth being low double digits.

Operator

There are no further questions at this time. I'll turn the floor back to Ms. Matthews for any final comment.

K. Darcey Matthews - *NCI Building Systems, Inc. - VP of IR*

Thank you, Melissa. To let everybody know, we're going to be attending the Seaport Global Securities Conference on March 22 in Coral Gables, Florida. And with that, we thank you for your time and your interest in NCI. Have a nice day.

Operator

Thank you. This concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation.