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Hyster-Yale Materials Handling, Inc. (HY)

Q3 2019 Earnings Call

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Joe L. Mondillo
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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by, and welcome to the Hyster-Yale Materials Handling 2019 third quarter earnings conference call.

At this time, all participants are in a listen-only mode. After the speaker's presentation, there will be a question-and-answer session. [Operator Instructions] .

I would now like to turn the conference over to your speaker today, Christina Kmetko. Thank you. Please go ahead, madam.

Christina Kmetko
Investor Relations Consultant, Hyster-Yale Materials Handling, Inc.

Thank you. Good morning, everyone, and welcome to our 2019 third quarter earnings call. I am Christina Kmetko, and I am responsible for investor relations at Hyster-Yale.

Joining me on today's call are: Al Rankin, Chairman, President, and Chief Executive Officer of Hyster-Yale Materials Handling; Colin Wilson, President and Chief Executive Officer of Hyster-Yale Group; and Ken Schilling, our Senior Vice President and Chief Financial Officer.

Yesterday evening, we published our third quarter 2019 results and filed our 10-Q. Copies of the earnings release and 10-Q are available on our website. For anyone who is not able to listen to today's entire call, an archived version of this webcast will be on our website later this afternoon and available for approximately 12 months.

I would also like to remind participants that this conference call may contain certain forward-looking statements. These statements are subject to a number of risks and uncertainties that could cause actual results to differ materially from those expressed in the forward-looking statements made here today in either our prepared remarks or during the following question-and-answer session. We disclaim any obligation to update these forward-looking statements, which may not be updated until our next quarterly conference call if at all.

Additional information regarding these risks and uncertainties was set forth in our earnings release and in our 10-Q. Also certain amounts discussed during this call may be considered non-GAAP. The non-GAAP reconciliations of these amounts are included in our earnings release and available on our website.

Now, let me discuss our third quarter results and activities. I will discuss the highlights first and then get into the details. Our 2019 third quarter consolidated revenues decreased modestly to $766 million from $783.9 million in last year's third quarter. Despite this decrease in revenues, our consolidated operating profit increased significantly to $19.5 million from $12.2 million last year. The Lift Truck business' 44% increase and operating profit was the driver of the substantial improvement partly offset by [indiscernible] (02:46) both Bolzoni and Nuvera.

The improved 2019 operating profit could not however counteract the substantial unfavorable change in income taxes as we recorded an income tax provision in the 2019 third quarter compared with a substantial income tax benefit in the prior-year quarter, which included a $5.5 million tax benefit from US tax reform. As a result, third quarter 2019 net income decreased to $12.8 million or $0.76 per share from $15.4 million or $0.93 per share last year.

Looking specifically at the Lift Truck business, Hyster-Yale Group's revenue decreased to $725.3 million from $740.8 million. Modestly higher revenues in the Americas predominantly generated by price increases were offset by revenue declines in EMEA and JAPIC. The overall decline in the consolidated Lift Truck revenues was primarily due to fewer unit shipments in all regions, mainly because of a continuing shortage of key components on certain part of the line products from key suppliers. These shortages also contributed to a change in the mix of products within the backlog, which resulted in a higher average sales price per unit in the 2019 third quarter. Lower bookings this quarter were partly a result of extended lead times on certain product ranges caused by the same supplier issues as well as reduced, but still robust market level.

Hyster-Yale Group's operating profit increased to $28 million in the third quarter up from $19.4 million last year, because of improved results in all three Lift Truck segments. In the Americas and EMEA, we were able to realize benefits from price increases as well as favorable retroactive tariff exclusion adjustments of $8.7 million from suppliers for certain components imported from China.

The lower operating loss in JAPIC was primarily the result of the absence of $4 million of unfavorable one-time purchase accounting adjustments made in the prior year associated with our acquisition of Maximal. These improved results were partly offset by the effect of lower unit volume, a shift in mix to sales of lower margin products, higher costs resulting from manufacturing inefficiencies mainly in the Americas associated with component delivery disruptions from key supplier and higher operating expenses primarily from higher product development cost to support our strategic initiatives.

At our Bolzoni segment, Bolzoni reported net income of $700,000 and revenues of $75.8 million for the 2019 third quarter compared with net income of $1.4 million and revenues of $84.4 million in last year's third quarter. Bolzoni's operating profit decreased to $700,000 down from $1.7 million last year, primarily due to costs related to the transfer of its North America operations from Illinois to Alabama including $500,000 of additional restructuring expenses.

Finally, at Nuvera, revenues increased to $2.4 million in the third quarter from $2 million in the prior-year quarter. Nuvera's net loss also decreased in the quarter to $5.8 million from a net loss of $6.4 million last year, primarily because of an accrued dividend from one of Nuvera's investments. Despite these improvements, Nuvera's third quarter operating loss increased to $9.3 million from $9 million last year, as a result of higher warranty expense and an increase in material cost.

Looking forward, we continue to focus on our six strategic initiatives and the many projects we are undertaking to execute these initiatives, which we believe will have a transformational impact on our competitiveness, market position and economic performance over the next three to five years. The longer-term outlook we established at the beginning of the year still generally hold, but we have made some adjustments as we have progressed through 2019 and begin to focus more closely on 2020 expectation.

Let me walk you through these updates. In total, the many projects we have discussed throughout 2019 have required and continue to require significant upfront expense and capital expenditure investment. We expect further increased investments to continue in the 2019 fourth quarter and to peak in the 2020 full year. We anticipate the capital expenditures will decline significantly in 2021, but remain at levels higher than 2019, while expensive investments are expected to generally remain at the 2020 levels for the next several years, excluding the impact of normal inflation.

While this quarter was one of increased investment, we believe the returns from these investments has started to be realized, and is expected to increase over the next five years. Before I provide an update on our financial outlook, let me provide some updates on specific more immediate projects and how those are expected to affect 2019 and 2020.

We've put the introduction of the first set of modular and scalable counterbalance trucks to occur in the second half of 2020 in certain markets. New lower-cost Class 3 walkie and stacker global products were launched in certain markets in the third quarter and are expected to be introduced in other markets during the 2019 fourth quarter. These products along with other new products launched earlier in the year are expected to have a significant impact on results in 2020.

The Hyster UT and Yale UX brand of Lift Trucks, a new line of high-quality and reliable, lower-intensity trucks for global markets and standard trucks for the Chinese market from Hyster-Yale Maximal will be launched globally beginning with the JAPIC, Brazil and Latin America markets during the 2019 fourth quarter and increasing over the course of 2020 to all countries.

We had previously noted that our China production activities were to be consolidated at the Hyster-Yale Maximal facility by the end of 2019. This transition will now occur in two phases with the first phase anticipated to be completed by the end of the year and the second phase expected to be completed by the end of 2020. We continue to add sales capabilities around the world, but we are also looking to reduce cost and other areas to contain spending.

Bolzoni has phased out its production at its Homewood, Illinois facility and substantially completed the shift of manufacturing to Sulligent. A distribution center and certain other operations are currently being maintained in Homewood.

In conjunction with this project, Bolzoni has recorded $2.5 million of restructuring charges thus far and payments related to this restructuring plan are expected to be made through 2020. In addition to the restructuring charges already incurred, Bolzoni anticipates that it will incur additional charges of approximately $800,000 to $1.5 million for the further restructuring-related costs during the fourth quarter of 2019 and into 2020.

The transfer of the responsibility for the development of non-fuel-cell engine components and the overall assembly of Class 1 and Class 2 battery box replacements to the Hyster-Yale Group is nearing completion. This will allow Nuvera to be entirely focused on fuel-cell stacks and engines by 2020.

Last quarter, we adjusted Nuvera's quarterly breakeven target due to a delay in shipments of engines for a key customer in China, resulting from the need for additional unplanned customer-driven product validation. Shipments are expected to ramp up throughout the second half of 2020, but if there are further delays with validation and production for this China customer, it may push out the breakeven date unless other opportunities currently being pursued are realized. Those were the highlights of the specific projects adjusted during the quarter.

Now, let me provide more information on the overall financial outlook. In summary, while the third quarter of 2019 reflect the continued investment in all of our programs, similar to what you saw in the first half of the year, we expect the fourth quarter to improve significantly in comparison to the 2018 fourth quarter loss realized last year. But still showing weakness, such as that were seen in the third quarter. Efforts we have taken to abate significant shortages from key suppliers in the United States are succeeding. However, while not fully resolved yet we expect these shortages to substantially ease during the 2019 fourth quarter and be resolved fully by the end of the year.

The status of tariff has been changing continuously, and although we are still experiencing significant additional cost from both the Section 232 and Section 301 tariffs, the Section 301 tariffs have been abated somewhat by granted exclusions and partly offset by our supply chain group securing alternative non-Chinese suppliers and negotiating price reduction. The exclusions were applied retroactively to the July 6, 2018 effective date and extend for one year after the notice of exclusions, or April 2020.

As I discussed last quarter, we recorded duties recoverable for the period of July 6, 2018 through the 2019 second quarter. This quarter we recorded additional recoveries from suppliers who provided components for which retrospective exemptions were granted. We anticipate some further, but substantially lower recovery in the fourth quarter.

In addition, our current Lift Truck backlog contains certain deal-specific pricing agreements at less than target margins to gain targeted account and for which margin improvement efforts have taken some time to mature. These agreements reduced our profitability in the first nine months of 2019. However, we expect margins to recover fully from both 2018 material cost inflation and the heavily discounted deals by the end of the 2019 fourth quarter. We also expect margins to continue to be enhanced by the exemption of tariffs on certain Chinese components. We have reduced the tariff surcharge [indiscernible] (12:49) products sold to customers. In this context, we expect operating profit at Hyster-Yale Group to improve considerably in the 2019 fourth quarter and full year over the comparable 2018 period and increase more significantly in 2020 over 2019 with improvements expected in each quarter over the respective 2019 quarter.

Further, improved results are anticipated with the significant increases through 2023. Our objective is to achieve our 7% operating profit margin target in this period assuming reasonable market conditions continue. We expect Bolzoni's operating profit to decrease substantially in the 2019 fourth quarter and full year primarily due to the restructuring of its Americas operations. However, as we get through the Americas restructuring results in 2020 are expected to significantly improve over 2019 with further improvements in the following years and a target of achieving the 7% operating profit margin.

Nuvera's results are expected to improve in the 2019 fourth quarter and full year over the comparable 2018 period, with breakeven targeted to be achieved in the fourth quarter of 2020. At each of these three businesses, the investments being undertaken are expected to lead to increase the operating profit through higher volumes, decreased product cost and improved pricing partly offset by a higher level of operating expense in future years.

As a result, overall we expect consolidated operating profit and net income in the 2019 fourth quarter and full year to increase significantly over the comparable 2018 period, excluding the impact of the $5.5 million tax benefit realized in the third quarter of 2018.

In 2020, consolidated operating profit and net income are also expected to increase substantially over 2019. Of course, the absolute profitability will reflect the actual market demand levels, which showed some softening in the first nine months of 2019. While markets are still at historically high levels, we believe the market is in a downturn, which is currently projected to be moderate and have limited duration. Therefore, in the remainder of 2019 and in 2020, we are currently forecasting strong but lower forklift market levels. We also continue to forecast a resolution to Brexit in a way that does not significantly harm our business prospects.

Before I open up the call for questions, I want to discuss a few balance sheet and cash flow item. Our cash position at September 30 was $62.8 million, up from $50.3 million at June 30, 2019 but down from $83.7 million at the end of 2018. Our debt balance was $351.1 million down from $370.9 million at June 30, but up from a December 31 balance of $301.5 million. The supplier constraints and the expenditures we are making associated with our strategic initiatives have significantly affected our cash flow and our working capital.

As a result of these factors, we expect our 2019 full-year consolidated cash flow before financing activities to decrease significantly compared with last year after you exclude the impact of the 2018 acquisition of Hyster-Yale Maximal which was a $78 million cash outlay.

Working capital is expected to improve significantly in the fourth quarter of 2019 as the inventory supplier issues are resolved, but we do not expect this improvement to fully offset the higher working capital experienced in the earlier parts of the year.

For the 2020 full year, we expect consolidated cash flow before financing activities to increase significantly over 2019.

That concludes my prepared remarks. I'll now open up the call for your questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] The first question comes from Joe Mondillo of Sidoti & Company. Your line is open.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC
Q

Good morning, everyone.

Kenneth C. Schilling
Senior Vice President & Chief Financial Officer, Hyster-Yale Materials Handling, Inc.
A

Good morning.

Christina Kmetko
Investor Relations Consultant, Hyster-Yale Materials Handling, Inc.
A

Good morning.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC
Q

Just one quick housekeeping question to start. The retroactive tariff exclusion income, what line did that hit? Is that on the gross profit line or SG&A or where did that hit exactly?

Kenneth C. Schilling
Senior Vice President & Chief Financial Officer, Hyster-Yale Materials Handling, Inc.
A

That's going to hit gross profit, Joe. It's essentially those tariffs were included in the cost of goods sold when we incurred them, so we reverse it through the same line.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC
Q

Okay. And then, I guess starting with the supply chain constraints, where do you see the timing of when we get back to sort of normalized levels? It sounds like the fourth quarter you'll start to see some improvements, but when do you sort of anticipate given what you are seeing that to sort of normalize?

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.
A

This is Colin. Basically now, around about now or certainly as we go through November and to December, it really it was centered around one key supplier. We had some minor issues with other suppliers. But it was one key supplier that supplies many of our castings, which ran into basically a capacity demand caused by some of our customers in that Class A truck business. That business is softened. We're sort of getting back on track with them fully right at this time. We have some clean-up to do. But generally, we see all of that being behind us as we go through the fourth quarter and we should be basically out of that issue completely by the end of the year.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

So, looking at sort of I guess the third quarter, this certainly I guess largely hits the Americas and I think the Europe had some issues as well. But the gross margins, if you exclude that tariff exclusion, retroactive income, gross margins right around 16% at the Americas segment. Is there any way you can – I don't know if you can quantify it. But how significantly did the supply chain constraints weigh on the third quarter gross margins?

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

Well, I mean it impacted in many ways. I mean it impacted in terms of our working capital, because we have a lot of semi-built trucks. A lot of components that we couldn't build trucks into. It affected our revenue because there was a significant number of trucks we couldn't get out of the door. And some of the each truck [indiscernible] (19:40) high-margin trucks. So, certainly, it impacted our margin. I mean, we had [ph] ships down (19:47) at our factories during the third quarter and then as the components became available we had to work overtime. So, it had a very significant impact on our operational performance.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

And has this affected at all demand? I assume most of your competitors are dealing with similar challenges. Do you feel like it has affected demand at all given the extended lead times and certainly the larger trucks?

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

We did have some cancellations. I mean, I wouldn't say major 100 – in the 100 range, 200 range during the third quarter. As far as the lead times now we sort of [indiscernible] (20:39) the line product, we're back to normal, with the 14 weeks. We do have some of the models that are impacted by the component shortage out about 5 weeks beyond that. But assuming we can manage. We also have been – we do have inventory in the field to our dealers that can help to dampen the peaks and troughs of demand. So, we're not concerned as we are in the fourth quarter about the impact of lead times, it certainly did impact our results in the third quarter.

Alfred M. Rankin
Chairman, President and Chief Executive Officer-Hyster-Yale Materials Handling; Chairman, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

However, to be absolutely clear, these extended lead times that were caused by the shortages, as a practical matter, probably did cause us to lose certain business on certain individual products...

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

Right.

Alfred M. Rankin
Chairman, President and Chief Executive Officer-Hyster-Yale Materials Handling; Chairman, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

...where the components were simply not available to produce within the time that people were willing to wait for the trucks, it was a very, very frustrating situation. And I would just add to what Colin said that we not only solved the issues with this particular vendor, but given their reliance on the Class A truck market they're not a good fit with us in many ways from a long-term supply point of view and so some of that's being moderated not completely, they were very good supplier, we will continue to work with them. But I would say that we have other suppliers as well so that we are going to ensure that we never get in this problem again.

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.
A

And part of the issue is sort of we were getting dates sort of when we were expecting them to get back to normal then they would miss those dates. And so, we were building our schedules around their promise dates and then we were having to re-promise trucks. So that did cause some frustration with customers during the third quarter. But I'll repeat what Al said, I mean, we're not going to allow it to happen again, so we're looking at sort of additional sources of the same components. But given the nature and given the number of components this supplier was supplying us with, it took us some time to get all that lined up, but we've secured against having the issue repeat as we move into 2020.

Alfred M. Rankin
Chairman, President and Chief Executive Officer-Hyster-Yale Materials Handling; Chairman, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.
A

Colin's point is a really good one, bringing new suppliers online to produce these components is a difficult task, and it has taken us quite a while to find the suppliers that are acceptable to us and our quality and their willing to take on this kind of business. I think Rajiv you would agree with that.

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.
A

Okay.

Alfred M. Rankin
Chairman, President and Chief Executive Officer-Hyster-Yale Materials Handling; Chairman, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.
A

Yeah.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC
Q

Okay. And then on the price cost side, I think you mentioned at least in the press release that you started to see a benefit from higher prices, so that price cost spread acted as a benefit in the third quarter. Do we continue to see positive trends in terms of price cost in the fourth quarter and into 2020, or was that sort of back to normal in the third quarter?

Alfred M. Rankin
Chairman, President and Chief Executive Officer-Hyster-Yale Materials Handling; Chairman, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.
A

I'll let Colin to elaborate a little bit, but I think it is back to where we wanted to be. In most cases, there is some additional benefit that will come through. But we feel that we accomplished some very important things. We took some business, as we said at the time, at the lower margins to build the confidence of customers that we have not done business with before. We feel that we have accomplished that. And at this point, we're not willing to continue to go forward in many cases with those relationships until we get a recognition of the value for money that we're delivering in terms of the profit of the product. So, I think we accomplished our purpose with some rather one-time decisions that we made to build long-term value in the business. But I think that process is pretty much behind us at this point. You want to say some more Colin?

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.
A

Well, I agree. Because of the extended lead time [indiscernible] (25:02) some of these lower margin trucks have bled into the fourth quarter, we were expecting them to be behind us in the third. But I'll summarize by saying I think we've been very successful on the pricing front in 2019, we've had to be because the cost situation has been very volatile and very arduous and – first of all, we have the impact of Section 232 tariffs. The economy was still going strong and suppliers were looking to pass price increases along, we're still incurring some impact I'd say about half the impact we were doing before from the Section 301 tariffs.

As the economy is softened, we've seen some softening of steel prices that have been coming down. Basically the hot-rolled coil and the flat plate almost at the same price it were before the tariffs were imposed, it's still much higher than they were when we saw the economy softened two or three years ago. So, our margins have improved. I mean, we have reduced the surcharge that we were applying, because we still are incurring some impacts from the Section 301 tariffs. But I applaud the Americas team, because I think they've done a very good job managing through all this and passing on our pricing into the market.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC
Q

And in terms of just the overall economy and the market slowing a bit, how is the product mix in terms of orders trended? Are you seeing more of a slowdown in your larger higher-margin type trucks? I'm just wondering amongst the different classes, how the order trends have trended?

Alfred M. Rankin
Chairman, President and Chief Executive Officer-Hyster-Yale Materials Handling; Chairman, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.
A

As you suggest, it does vary product category by product category. Again, Colin can elaborate it a bit more. Some of the sharpest downturns have been in products which are not our strength in the warehouse-type product areas, some markets for Class 2 forklift trucks. But there's also as you would guess from just reading about the general economy and the industrial activity that some of the industrial customers who are in the heart of the line for us are no longer buying at the rates that they were, they're coming back to more normal rates. Another way to think about it is that coming off the downturn probably 2011, 2012, 2013, 2014 people replaced a lot of trucks that they had deferred replacing. And by the time you got to 2019, most of that replacement activity that was pent-up is completed. So, now we're back to a more normal cycle is a way I would tend to think about it when people – [ph] they're more in our (28:18) normal replacement cycle. They haven't extended out the life because times are terrible. And so, there is some downturn, but there are also some signs that the market is picking up in certain areas. So, it's a very mixed set of signals out there. At this point, we think there were some action that was related to purchases in anticipation of the tariffs to try to purchase at more favorable prices before the inevitable price increases came through. Anything else you want to add to that Colin?

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.
A

Key market for us is North America. North America actually increased slightly in the third quarter over the comparable period of last year. First two quarters were – first quarter was down significantly, second quarter down not so much and third quarter actually showed a pickup, a small pickup. If you look at the European market, I mean, that's down around about 7.5%. All classes combined, some markets have impacted more than others. Germany is a key market there and I think last time I looked at the numbers, they were down sort of double-digits.

But, overall, we see – I concur with everything Al's said. I think we had a surge because of the anticipated inflation and tariffs and things are more back to normal in North America. We are watching very closely Joe the market by segment. Big trucks are very important to us, so we're looking at that very carefully [indiscernible] (29:55) segment. But [indiscernible] (29:57) nothing any of them trending down [indiscernible] (30:01) customers are little bit more cautious in some areas like customers in other areas more bullish. I mean, steel is – the steel market is still going strong. You're right. I think we just – we're cautiously optimistic about the North American market basically stabilizing at around about normalized 2018 levels as we go through the balance of 2019 into 2020.

Kenneth C. Schilling
Senior Vice President & Chief Financial Officer, Hyster-Yale Materials Handling, Inc.

A

Yeah. Joe, if you look at our average sales price in our backlog and what we booked, we had about a $3,000 increase in the average unit value that we booked in the third quarter over the second quarter. We still have a relatively high value in backlog primarily related to those trucks that we weren't able to bill, that were the premium trucks that have higher average sales prices. So that's still in the backlog and the backlog is still at a level higher than our average sales price and the bookings. But I think that the trend was a good trend in terms of average sales price in the third quarter compared to the second quarter.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

And when you – in terms of that comment, are you referring to the orders book or – because I understand the backlog, because you weren't able to get some of those higher-margin trucks out the door that those are still sort of propping up that value back – the backlog value. What about in terms of the orders book, was that also pretty positive in terms of orders on a value basis?

Kenneth C. Schilling
Senior Vice President & Chief Financial Officer, Hyster-Yale Materials Handling, Inc.

A

[indiscernible] (31:32).

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

I would say it was pretty normal.

Kenneth C. Schilling
Senior Vice President & Chief Financial Officer, Hyster-Yale Materials Handling, Inc.

A

Yeah. I was just trying to give you some numbers based upon the unit shipment booking and backlog table we have in the earnings release and we saw an increase in the average sales price in the trucks we booked in this quarter over last quarter.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Okay. What about when you look at the market growth? You're doing a lot of different things to try to drive the share gains. When you look at the market growth relative to your growth, what does that say to your share gain strategy?

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

Well, share gain strategy is done very much by industry segment. And so, we're looking at each individual segment, our strategy is to address each. We have themes, dedicated themes aimed at the different market segments. I don't think there's anything materially changing at this moment in time that would cause us to adjust our approach to the market. We're very strong in the counter-balanced products. Now, we have more opportunity in the warehousing products. We have launched some new products. We have some new products getting ready to launch. But also the effort of our industry sales teams and industry support teams are really focused on bundling together all of the activities necessary in order to sell these excellent products into the market and we're doing it with some success. And we expect that success to increase as we fully launch on all of our initiatives.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

And in terms of new products, I believe Christy at some point said something like new products are going to make a significant impact on 2020. Was that referring to primarily Maximal or is that a general comment of new products for the company in 2020?

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

Well, I think it's a multiple new products coming along. Certainly, we see global potential for the Maximal build Hyster-Yale UT and UX. These are very – they're high-reliable, good-quality, very cost-competitive trucks that really serve the low-intensity markets. We have new Reach Truck coming out which we think is the best – in North America, which we believe will be the best product on the market. And then, we have as we go through 2020, we start launching our new modular and scalable counterbalanced range IC engine and electric that would be hitting the market as we go through 2020, which we think will be a real winner for us in the market. It's a huge product development program that's been in the making for several years now and we will be launching the first of those trucks around about mid-year 2020.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Okay. And then...

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

And then [indiscernible] (34:45) the trucks we launched in 2019 that we expect to really gain momentum as we go through 2020.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Right. And then just going – moving to sort of expenses, I understand that you're continuing to invest for the long-term and you're going to see some areas where expenses are rising to invest in these long-term initiatives. You also mentioned in the prepared commentary I believe that you're trying to find other areas of the cost structure to offset some of that. How do we think about how much costs have been rising over the last year or two, and at what rate does that compare in 2020? Do some of these offsets slow that increase in 2020? Or I'm just trying to understand how much of a headwind of near-term higher costs?

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

As you look at 2020, I think the level of general expenses that we have at this moment in time, if we're not at peak, we're close to peak. Clearly, we've got sort of general inflation happening that will impact our cost structure. But we've just completed a series of reviews with the divisions and been spending a lot of time talking about the redeployment of resources or what can we do to – how can we sort of change the structure to fee or paid account to apply to the various initiatives. I mean, one of the key initiatives is having a lot more frontline salespeople in various theaters around the world. What do we have to do to find the offsets to fund that activity? So, again, I'll repeat if we're not at peak levels, we're very, very close and then we expect that level to be sustained, but we expect the percentage SG&A to go down as our revenues rise.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Okay. And then...

Kenneth C. Schilling
Senior Vice President & Chief Financial Officer, Hyster-Yale Materials Handling, Inc.

A

And, Joe, we're getting close to that annualization point where we have – we've now annualized the changes in headcounts in, and that'll happen you have this year and then going in the next. As Colin pointed out, we'll be at a more steady state with just normal puts and takes that you'd expect in an SG&A line.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Okay. Specifically at the JAPIC segment, I understand that there's a lot of investments going on there and you're still on profitable levels there, do you anticipate a pretty big improvement, or when do you think you can sort of get to profitable levels at JAPIC?

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

So, I mean, we have to remember, we only acquired Maximal in middle of last year and we're going through a significant period of reengineering of that facility. We bought a very good company with very good people and a good location. But we're having to do a lot of work to bring it up to the standards of our factories around the world, introducing DFT, putting in place the right level of people in the right positions. We're putting in a new SAP system into the operation. We're transferring our production out of Shanghai into that facility. So, we're still incurring a lot of cost associated with all of that. But in terms of the performance of the operation, the call operation, it's doing very well; and comparing how we're performing against our business [ph] base (38:45), I would say we're ahead of schedule, in terms of what we expected to happen.

Once the Maximal facility gets fully up to lead, which we expect to happen over the next 12 months or so, it will transform the profitability of the JAPIC region, because that will become the major source for much of the trucks – much of the product that gets sold in that market.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Okay. And then a few questions on Nuvera. You briefly mentioned about the engine validation that you're still waiting on, any more color in terms of timing on that or is it just uncertain given that it is sort of governmental based?

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

I think we said everything in the release. We've got a very good partner. We have to do some work to get the engines such that they can be really sold in high volumes to multiple customers through that partner and beyond that, I think everything is said in the release.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Okay. So, looking at sort of the cadence or the sort of revenue, I'm just wondering, you have a couple of contracts there; it's not just the one where you're waiting on the engine validation. Do you anticipate – when do you anticipate revenue to start to ramp up? Is this going to be more of a back half of 2020, or do you think you can see improvement in the first half of 2020?

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

Well, I mean, obviously as we start shipping the engines in quantity the revenue will start ramping up. So, the revenue is tied to the comments I just made.

Alfred M. Rankin
Chairman, President and Chief Executive Officer-Hyster-Yale Materials Handling; Chairman, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

And it does ramp up through the course of 2020.

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

Right. I mean that is the key determinant, the determining factor as we look at the fourth quarter and the revenue and margin from that contract. And again, there are obligations on behalf of the Chinese partner. So and as much as we can ship the number of units we have in the schedule, we'll achieve the breakeven. If for any reason, there's a delay then that will push the breakeven out.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Okay. And then on the battery box replacement side, what is the update on the production move to Greensboro (sic) [Greenville] (41:24), is that all situated at this point?

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

It is. I mean, we're producing in Greenville and I have to admit in relatively low numbers at this moment in time, but we're probably going through a ramp-up period, as we speak.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

And when does that...

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

But all of the production – all the production for the Class 1 and Class 2 products have been moved to Greenville. The Class 3 product is still being produced in Billerica at this time.

Alfred M. Rankin
Chairman, President and Chief Executive Officer-Hyster-Yale Materials Handling; Chairman, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.
A

One of the things I think I'd say that perhaps isn't outlined in much detail in the earnings release is that at Nuvera we have – because we're commercializing a developmental product as you would expect, there are a number of things that we run across that happen in the field as the units are deployed. We feel that we've addressed all of those issues from an engineering point of view, but we still have some work to do to get them all implemented in the field and most importantly bring down the cost, the warranty costs associated with those products and give – put our best foot forward with our customers by having products that are operating according to fully developed commercial standards. If we can do that we'd be the only one in the industry. And that's our objective. But we've got a task to do, I would say, over the next couple of quarters to get our – all of our engineering fixes implemented in all the boxes in the field and then the producing products which incorporate all of those engineering improvements. So, over the next couple of quarters, we've got some things to clean up that will benefit both the cost structure in the long-term and customer satisfaction which is probably the most important of the two in the long-term.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC
Q

Has the battery box replacement accounting moved over to the Americas segment [indiscernible] (43:52) or is it still baked in the Nuvera?

Kenneth C. Schilling
Senior Vice President & Chief Financial Officer, Hyster-Yale Materials Handling, Inc.
A

Joe, we've got the Class 1 and Class 2 product as well as the distribution of BBRs is handled by the Americas. The fuel-cell engines and the assembly of the Class 3 BBRs is still in Billerica.

Alfred M. Rankin
Chairman, President and Chief Executive Officer-Hyster-Yale Materials Handling; Chairman, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.
A

And the financial reporting is in accordance with that division of responsibility.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC
Q

Right. The new generation of – I think you're introducing a second generation of battery box replacements that's supposed to be better designed. Has that been introduced yet or what's the timing on that?

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.
A

First quarter of 2020. So, it is a new design. It's lower cost. We're very optimistic about the prospects.

Alfred M. Rankin
Chairman, President and Chief Executive Officer-Hyster-Yale Materials Handling; Chairman, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.
A

The only caveat I would give you is the one that we would have for any product, which is that as the new product comes in, we want to make sure that we have a thoughtful and sensible phase-out, phase-in program so that we don't have excess inventory that we have to write-off. So, there may be some period, we're looking at right now to make sure that we sold out all the inventory of components and balance things out, as best we're able before some of those new products come up to, what I would call full production at this point. So that process will be going on in the first half of the year or so.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Okay. And then last question on Nuvera, potentially sort of related to your last answer there, Al, the supply chain trying to improve the supply chain and the economics of the supply chain. How is the progress been going with that?

Alfred M. Rankin
Chairman, President and Chief Executive Officer-Hyster-Yale Materials Handling; Chairman, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

Well, the intensity of the effort being put into that continues at the highest possible level. We certainly have in place the capabilities that we need through 2020. But we are continuing to work to – with our current suppliers, develop additional suppliers, do all the things that would be normal to ensure that as the volume goes up, we come down the cost curve. And that process is actively underway. We have brought to bear not only the purchasing capabilities of Nuvera, but we've supplemented them with some of the expertise we have in our Lift Truck business and supplier development and quality control. And I think Colin may want to add a couple of things to that.

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

Also, investing some of the capital expenditure, I think we might have called that out is to do with the equipment to automate a lot of things that are done manually which will significantly reduce the cost of assembling.

Alfred M. Rankin
Chairman, President and Chief Executive Officer-Hyster-Yale Materials Handling; Chairman, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

That process is underway, as we speak in Billerica. I think it's basically in a position of proving out the machinery, everything seems to work adequately in the suppliers' plants and that's being debugged now. And when we are fully satisfied with those capabilities we'll also be having parallel production capabilities in China with the same automation. We want to do it – wanted sequentially so that we build on – we have absolutely everything working the way we wanted to well it's here in the United States and we'll put it in place in China, because we need to be close to our customers and we need to have the lower costs that are associated with the Chinese production. So, we're doing that in conjunction with the rented space from our Maximal business that will give us the oversight and control and mass in China and ensure the success of that program.

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

And we have an Investor Day coming up in New York in just a few weeks' time and we'll be going into all of this in a lot more detail and talking about our China plans in a significant amount of detail.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Okay. And then, one question on Bolzoni. If you exclude the restructuring, the operating profit is down year over year and certainly the margin even excluding the restructuring costs are not close to your sort of long-term targets. How much has the – what you're doing in terms of moving the production in North America weight on that and sort of just help me understand the operating margins there and what you're expecting in 2020 [ph] as is (49:29)?

Colin Wilson
President and Chief Executive Officer, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

If you look at the Bolzoni business, North America at this moment in time is very small part of our business. So, yeah, we're incurring a lot of costs. We expected to be a much bigger part of our business as we move into the future and ramp up our production in Sulligent and really do a lot to increase our market penetration. Bolzoni's biggest market is in Europe. The Europe market is down with the Class 1, 2 and Class 5 is down, which is where most of the attachments get sold all is down 7.5%. Having said that, they've been increasing their sort of penetration. What really hurts Bolzoni more than anything is the currency translation from euros into dollars. And I think if you normalize all of that out and sort of take out a couple of sort of one-time things that happened [indiscernible] (50:24) concerned about the underlying performance.

Alfred M. Rankin
Chairman, President and Chief Executive Officer-Hyster-Yale Materials Handling; Chairman, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

Yeah. But there's another facet of this, which you have to I think make sure that you get fully calibrated and that is that there is the core Bolzoni traditional business, which is what Colin was just addressing. But Bolzoni has also taken over responsibility for certain other kinds of components than attachments that are used in the forklift truck business and it's our objective to sell those more broadly to other competitors in the forklift truck industry. And so for example cylinders, but in the context of this transition that is a low-margin business, the way it's being handled financially. So, you're not seeing a clean set of numbers and we're doing a fair amount of outsourcing in conjunction with this program. So, in totality, what we will see is a phased improvement in the margins in North America that comes from improvement in both the traditional business of Bolzoni and that is the core business. And this additional component supply business that is currently in place, some of which is associated with the phase-out of our current generation of Lift Truck products. So, there's quite a bit of other activity that affects the North American margins in the short-term. But from an operational point of view, this is a much better way for us to be positioning the business. So that kind of clouds the understanding a little bit.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Okay. Great. And then last question just on cash flow. In terms of your inventories, how high are your inventories from sort of normalized levels? I'm just trying to understand over the course of the next 12 to 18 months, how much inventory could potentially be a positive for cash flow.

Kenneth C. Schilling
Senior Vice President & Chief Financial Officer, Hyster-Yale Materials Handling, Inc.

A

Hey, Joe, I think the way to look at that is, we typically target roughly around 15% of sales for total working capital. At times, we end up with pockets of heavier inventory and maybe lighter receivables. That's somewhat the case today because of the supplier constraint issue. We expect as we work through the supplier constraint to get back to a more normalized levels of production and inventory levels that would match the volumes. But you got to remember, we're a volume-driven business from working capital, so as we put more units into play in production schedules in the future, we're going to need working capital to fund those. And as we see volumes come down, we would get it back out. And we also have programs to enhance working capital generation that we're managing as well along with kind of the normal volume-driven elements of working capital. But we do have this distortion right now from [indiscernible] (54:02).

Alfred M. Rankin

Chairman, President and Chief Executive Officer-Hyster-Yale Materials Handling; Chairman, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

A

Ken is really – we're actively – really focused on the right thing. We're actively focused on managing the working capital and bringing the numbers in the line. But I think it's fair to say that receivables are pretty much in line with where we would expect them to be that inventory days outstanding have been higher pretty much throughout the year because of the problems with [indiscernible] (54:30). And I would expect it as we go into 2020 as opposed to being in the fourth quarter that that would begin to come back into line that sort of 10% lower than the numbers that we're seeing now. And that is on a days outstanding basis. So, I'm not talking absolutes. I'm talking days outstanding. And at the same time as probably it won't surprise you, our payables are actually going down and we expect that they'll go down in the fourth quarter as the inventories are starting to write themselves and we're then buying less. So, we're going to go through one of those odd periods where in the fourth quarter as a part of the process of right-sizing the – and balancing all three components of working capital, we're going to have a little decline in the payables and then as Ken said, it pretty much comes into balance in our more traditional days outstanding by the time we get into 2020.

Joe L. Mondillo

Analyst, Sidoti & Co. LLC

Q

Okay. And then just lastly related cash flow still. CapEx, what is your anticipation for this year? And I know because you moved some of the CapEx spend related to the modular production into 2020, just was trying to get an idea of what your CapEx will be like for 2020.

Kenneth C. Schilling

Senior Vice President & Chief Financial Officer, Hyster-Yale Materials Handling, Inc.

A

Well, I think the guidance we gave – I guess the way to say this Joe is we started out the year with $79.1 million was going to be our CapEx for the full year – sorry $76.5 million for full year. We're now at an estimate of about $55.9 million, which is what's in our Q. We have a large chunk of that in the fourth quarter. So, we've got a lot of activity just to get that done and the spend and put in place. But the reduction you've seen in 2019's forecast with CapEx will move over into 2020's and our guidance clearly has this 2020's CapEx will increase fairly significantly. And then we'll begin to drop down as we go forward in years.

Joe L. Mondillo

Analyst, Sidoti & Co. LLC

Q

Okay. Great. Thanks a lot. Appreciate it. Thanks for taking my questions.

Christina Kmetko

Investor Relations Consultant, Hyster-Yale Materials Handling, Inc.

A

Thank you, Joe.

Operator: And this concludes today's question-and-answer session. I will now turn the call back to our presenters.

Christina Kmetko

Investor Relations Consultant, Hyster-Yale Materials Handling, Inc.

Great. Thank you very much for joining us today. Does anybody want to add anything to wrap up?

Alfred M. Rankin

Chairman, President and Chief Executive Officer-Hyster-Yale Materials Handling; Chairman, Hyster-Yale Group, Hyster-Yale Materials Handling, Inc.

I guess I'd just say that the overall perspective is, there have been a lot of cross-currents between tariffs and supply chain and restructuring and short-term market disruptions and pre-buying and a whole variety of things. And as we've indicated that fourth quarter is going to be a better quarter than last year, but we are not focused on the fourth quarter as the time is going to be really robust. And what we are focused on is 2020 when we think that a lot of the pieces are coming back together. And at least as we see the market and our market position and the impact of the new products, we have a very positive point of view about 2020. So that's kind of the summary perspective that I would have at this point. I just leave it at that, the, Christy.

Christina Kmetko

Investor Relations Consultant, Hyster-Yale Materials Handling, Inc.

Great. Thank you very much. We don't have anything else here.

Operator: Thank you for participating in today's Hyster-Yale Materials Handling 2019 third quarter earnings conference call.

This call will be available for replay beginning at 2:00 pm Eastern Time today through 11:59 pm Eastern time on November 6, 2019. The conference ID number for the replay is 8366818. Again the conference ID number for the replay is 8366818. The number to dial for the replay is 800-585-8367, or 855-859-2056, or internationally dial 404-537-3406. You may now disconnect.