

Spartan Motors, Inc. [SPAR]
Investor Call
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Company Representatives:

Juris Pagrabs; Group Treasurer, Director of IR
Daryl Adams; President, CEO
Rick Sohm; CFO

Analysts:

Jordan Bender; Seaport Global Securities
Ryan Sigdahl; Craig-Hallum

Presentation:

Operator: Good morning and welcome to Spartan Motors' conference call to discuss the acquisition of Smeal Fire Apparatus. (Operator Instructions) Please note that this event is being recorded.

I would now like to turn the conference over to Mr. Juris Pagrabs, Group Treasurer and Director of Investor Relations of Spartan Motors. Please go ahead, sir.

Juris Pagrabs: Thank you, Allison. Good morning, everyone, and welcome to today's conference call to discuss the acquisition we announced yesterday morning. Joining me on the call today are Daryl Adams, our President and Chief Executive Officer, and Rick Sohm, our Chief Financial Officer.

Yesterday, Spartan Motors announced the signing of a definitive agreement to acquire Smeal Fire Apparatus, an industry-leading innovator and manufacturer of fire apparatus in North America. The transaction is expected to close in January 2017, subject to certain closing conditions.

For today's call, we've included a presentation deck which was filed with the SEC and is also available on our website at spartanmotors.com. Please navigate to the Investor Relations tab and then Webcasts and Transcripts to find this presentation. For more information on the Smeal transaction, please visit spartanmotors.com/smeal.

Before we start today's call, please go to slide 2 of the presentation for our safe harbor statement. You should be aware that certain statements made during today's conference call, which may include Management's current outlook, viewpoint, predictions and projections regarding Spartan Motors and its operations, may be considered forward-looking statements under the Private Securities Litigation Reform Act of 1995.

I caution you that, as with any prediction or projection, there are a number of factors that could cause Spartan's actual results to differ materially from projections. All known risks that Management believes could materially affect the results are identified in our Forms 10-K and 10-Q filed with the SEC. However, there may be other risks that we could not anticipate.

At this time, I'd like to turn the call over to our CEO, Daryl Adams, for his opening remarks which begin on slide 3.

Daryl Adams: Thank you, Juris. Good morning, everyone. Thank you for joining us to discuss our exciting announcement.

I'd like to begin by sharing how pleased we are to be here to discuss this significant milestone in our company's history, particularly as it relates to our emergency response business unit. It's our goal today to lay out for you all of the many opportunities for value creation that this acquisition brings to Spartan Motors.

This transaction combines two leaders in the emergency response industry, Spartan Motors and Smeal Fire Apparatus. The new and combined company will rank as a top four North American fire apparatus manufacturer, with a robust and respected portfolio of industry-leading products, and will be well positioned in an increasingly consolidated industry with a broader geographic reach for a more robust network of dealers.

Through increased capacity utilization the new company will double its full apparatus production and leverage its strengths to accelerate the emergency response business unit turnaround plan and be accretive in 2017 results.

Please turn to slide 4 of the presentation. Founded in 1955, Smeal is a \$100 million manufacturer of fire apparatus, with sales primarily in the U.S. and Canada. Smeal operates facilities in Snyder and Neligh, Nebraska; Delavan, Wisconsin; and Ephrata, Pennsylvania. Smeal has approximately 400 employees, has four operating facilities, and will add 25 dealers in 40 states, 10 provinces, and 3 territories in North America.

Spartan Motors has a long-lasting relationship with Smeal as its cab and chassis supplier, which dates back 30 years. Further extending and cementing that relationship, it is a natural progression for the two companies.

Smeal and its subsidiaries, U.S. Tanker Company and Ladder Tower Company, are established industry leaders and innovators in fire truck manufacturing and vehicle technology, offering a full line of aerial ladders, platforms, and tractor-drawn aerials, as well as a wide variety of custom and commercial pumpers and other emergency response vehicles.

Well known trademarked products such as the Sqrurt, TeleSqrurt, and Snorkel set Smeal apart in the industry and provide an immediate path to new innovation and expertise.

Just like the approach of our own Spartan Motors emergency response business unit, Smeal is focused on delivering state-of-the-art technology, innovative engineering, and rock solid

durability in each and every one of its products. Smeal brands and products have a strong heritage, superior customer loyalty, and a well defined position of strength in the market. In combination with our existing products and brands, I truly believe we have built the preeminent collection of emergency response products and vehicles that will continue to get even better over time.

Turning to slide 5, we believe that there are numerous compelling reasons for bringing together these two industry leaders.

The emergency response industry, like many others, is consolidating. With this acquisition, Spartan Motors will increase its competitive position while at the same time ensuring that healthy competition remains and that our customers and dealers will have a wide variety of better, not fewer, choices.

When this transaction is complete Spartan Motors will rank amongst the top four North American companies that manufacture and market fire apparatus and vehicles.

One of the most appealing aspects of this deal is the ownership of Smeal's industry-leading product portfolio and innovation expertise. Notably, Ladder Tower Company has been designing and selling aerial products for more than 45 years, with more than 5,000 aerials sold. For context, Spartan has been selling aerials for approximately 10 years now. Together this combined engine expertise, manufacturing expertise, and solid dealer channel reach accelerates our ability to better service the fire industry.

Not only will this diversity expand our product portfolio, we will increase our dealer network to provide coverage in 44 states in the U.S. and 10 provinces throughout the U.S. and Canada, while distributing the Company's products in more than 11 other countries around the globe.

The entire ER team has been diligently focused on turning around our emergency response business unit over the past year. Our business unit's operational leadership has ramped up over the past 12 months to a new standard.

I'm pleased to share that Spartan's emergency response operational leadership team carries with them a combined 120-plus years of direct emergency response industry expertise. The team has taken several significant steps forward in our turnaround plan this year, where we see that experience working in our favor firsthand.

With the acquisition as an acceleration of that positive momentum, the possibility of two highly qualified leadership teams converging was an important factor in Smeal's desire to join Spartan and our own confidence in doing this deal. The entire Spartan Motors team is looking forward to working very closely with Smeal's operational leadership as we bring new product development resources and innovation to our dealers, while simultaneously bringing our customers together so they may create additional value.

At this time I'd like to turn things over to our Chief Financial Officer, Rick Sohm, to discuss the financial aspects for the transaction.

Rick Sohm: Great, Daryl, and good morning, everyone.

Please turn to slide 6. As Daryl described, we couldn't be more excited to bring these two strong companies together, and we're highly confident in our ability to generate meaningful incremental shareholder value by accelerating the turnaround of Spartan's emergency response business unit through this combination.

As we said earlier, we've entered into a definitive agreement to acquire the assets of Smeal and its subsidiaries for approximately \$36.3 million in cash, subject to certain working capital adjustments and forgiveness of certain liabilities owed by Smeal to the Company, which total approximately \$5.7 million as of December 12, 2016, and a subsequent tax gross-up payment which is not expected to exceed \$2.4 million and which is expected to be more than offset by tax benefits of approximately \$3.8 million accruing to the Company.

Smeal is expected to generate positive EBITDA in 2016, and once the deal is completed it is projected to be accretive to Spartan Motors earnings in 2017, driven primarily by a combination of higher volumes, increased operational efficiencies, and other synergistic opportunities.

As Juris mentioned, the transaction is expected to close in early January 2017. We expect to report our 2016 earnings in late February and at that time we anticipate providing 2017 financial guidance, which will reflect Smeal's expected contributions on a consolidated basis.

The deal will be initially financed through our recently amended \$100 million line of credit. As we indicated on our third-quarter conference call, we ended Q3 with \$90 million in total liquidity, consisting of \$40 million in cash and \$50 million in borrowing capacity under the revolver.

Our liquidity position has improved since that time and after closing this transaction our balance sheet will remain strong. We will have sufficient funds to support our working capital requirements, as well as continuing to be opportunistic in our capital allocation. Overall, we feel comfortable with our capital structure going forward.

We believe there are numerous opportunities to evaluate best practices across the combined Company's operations, including the implementation of Spartan's production system and lean manufacturing initiatives, that will drive operational improvements and increase profitability.

As Daryl mentioned, we believe this transaction will bring significant scale to our emergency response vehicle portfolio by increasing revenue by more than 35%, which will help accelerate the turnaround of the Spartan emergency response business unit, which has been our number one priority. As we've stated in past earnings calls, we expect our current ER segment to be profitable on a run rate basis by the end of 2017. We believe this combination will allow us to accelerate that timetable.

Now we should move to slide 7. I wanted to share a few more details about the combined Company's financial profile. As a reference we've provided Spartan's 2016 midpoint guidance for comparability.

We expect Smeal to end 2016 with approximately \$100 million in revenue. And please keep in mind that includes approximately \$30 million of Spartan chassis revenue sold to Smeal that will have to be eliminated when the companies are consolidated. In 2017 we expect Smeal to add more than \$70 million in incremental sales for the combined Company.

We expect Smeal to generate approximately \$0.5 million of EBITDA in 2016, which is not truly indicative of future profits, as their second-half 2016 run rate is higher than the first half.

The team at Smeal has been working hard on improving their profitability, much like we've done in our own ER business over the last year. And we expect to continue to improve on that run rate going forward.

At this time I'll turn the call back over to Daryl for his closing remarks.

Daryl Adams: Thank you, Rick.

Please turn to slide 8. It clearly demonstrates the before and after footprint of Spartan Motors' expanded dealer network. This view of the combined Company's dealer channel reach across the United States and Canada underscores our position as one of the most significant players in the emergency response industry.

The transaction drastically expands our distribution network, doubling our complete apparatus sales reach, particularly in Canada where Smeal's dealers have had a long-lasting superior presence.

Turning to slide 9, we look at a global footprint that continues to grow. Smeal brings to the table a very strong presence in Canada, alongside Spartan which already distributes its emergency products in 11 countries. Combined, the new company will increase its dealer network to provide coverage in 44 states and provinces throughout the US and Canada, while distributing the Company's products in more than 11 other countries around the globe.

While global expansion has happened organically up to this point, our new, more significant scale, coupled with an industry-leading product portfolio that boosts true aerial dominance, we're now well positioned to aggressively pursue our global expansion plan.

Of course the completion of the turnaround plan for Spartan Motors' emergency response business unit remains top priority. We're mindful of the fact that we need to take the time necessary to fully integrate Smeal. We see expanding our international presence as a longer-term goal of the new emergency response business segment, and an initiative that can be scoped concurrently.

This leads us to slide 10 and a discussion of the expected benefits that will result from our acquisition of Smeal.

From an organizational structure standpoint, we are exceptionally pleased to be adding the Smeal operational leadership team to Spartan. We have spent a lot of time with the Smeal team and we believe our company cultures are an excellent cultural match. We very much look forward to partnering with the Smeal team and working with them shoulder to shoulder.

Once the deal closes and the integration efforts get fully underway, we expect to work hard to implement best practices across the operations of both companies. We will be looking at how to best utilize our capacity and design and manufacturing expertise. Bringing our design and engineering teams together and leveraging our talent will give the Company an advantage over our competitors and also provide the opportunity to invest in new product innovations that will drive future business.

With the addition of Smeal we become one of the largest manufacturers and marketers of fire apparatus. We firmly believe our combined product portfolio is one of the best in the industry.

Slide 11 underscores the powerful combination we see as a result of bringing Spartan Motors and Smeal together as one company.

Smeal's leading product portfolio, aerial dominance, and manufacturing expertise solidifies Spartan's place in the market and positions us for expanded market penetration in the form of innovative, industry-leading products and larger customer base and a much broader geographic reach.

Finally, this is a deal that we believe will position Spartan Motors for an accelerated turnaround of our emergency response business, which will deliver value to our shareholders.

In conclusion, we expect that our operating discipline, leveraged infrastructure, and integration opportunities will drive improved performance in our new, larger emergency response organization. We do believe this transaction can be a game changer for Spartan's emergency response business unit and ultimately Spartan Motors shareholders.

We are excited to execute on all the opportunities in front of us. With this transaction we gain more than a well respected company and its brands. We gain the expertise, engrained knowledge, and the aerial DNA of the talented people who built the Smeal business and who will add new skill sets and bring new perspectives to our combined organization.

We look forward to welcoming the Smeal team into the Spartan Motors family and to the infusion of talent and ideas that will follow.

Operator, we're ready to take questions.

Questions & Answers:

Operator: Thank you. We will now begin the question-and-answer session. (Operator Instructions) Mike Shlisky; Seaport Global.

Jordan Bender: Good morning. This is Jordan Bender on for Mike this morning. You kind of went over some of the synergies as part of this deal. I was wondering how much do you think you can gain from the sales and distribution standpoint beyond that \$70 million by combining the companies, and how much might come from cost reductions.

Rick Sohm: Yes, I think, Jordan, we appreciate the question. I think we see opportunities both on the revenue side for the increased distribution and sharing of the product portfolio across the dealer network. And we also see cost opportunities. So we think they're significant in both cases.

And I think, like we said in the discussion, we're working with the team pretty closely and I think we'll be able to lay out how 2017 will unfold when we have our earnings call in February.

Jordan Bender: Okay. And I was wondering if you have a sense of what your amortization costs might be. And were those included in your accretion assumptions?

Rick Sohm: I think when we look at that, Jordan, yes, those are included in our comments around the accretion of 2017 earnings.

Jordan Bender: Okay. And is Smeal a growth company right now? Or what part of the cycle was it in?

Daryl Adams: Yes, Jordan. This is Daryl. Yes, Smeal is in a growth cycle right now. We're looking at their present capacity and they've been on an upward curve. So we see some benefit in 2017 and throughout 2018 and going forward in their production. Obviously some of their products we'll probably move around to get to some focused factories. But that's all to come through 2017. But, like Rick said, we see it being accretive in 2017. So we're excited about the opportunities in front of us.

Jordan Bender: Okay. If I could sneak one more in here, was this deal an auction process? And were there any other potential buyers involved?

Daryl Adams: No, it was not an auction process. And we're not aware of any other buyers that were involved.

Jordan Bender: All right. Appreciate it. Thank you.

Operator: (Operator Instructions) Steve Dyer; Craig-Hallum.

Ryan: Good morning. It's Ryan on for Steve. Thanks for taking our questions and congrats on the acquisition. Kind of going along with Jordan's last question, just hoping you could talk about the acquisition. It's a little bit earlier than we were expecting. What are you guys seeing in the market? What's your current pipeline? And then, any capital allocation plans going forward?

Daryl Adams: Yes. So, Ryan, I'll talk about the pipelines and I'll let Rick take the capital.

So the pipeline -- both of our backlogs are nicely where we want them to be. We just looked at -- our ER business is turning around. It's going to be profitable by this year, by run rate near the end of the year. So it is a little earlier than what we announced, but the opportunity came up and we just wanted to be opportunistic.

And we love their products. I think that's part of the key, was the products we gained. The Squirt, TeleSquirt and the Snorkel are also loved internationally. And it's something that will play into our global expansion as we get down to mid to longer term.

So at this time we thought it was a good opportunity. Especially with the industry starting to consolidate, we just wanted to be opportunistic. And this came on the market. Even through our long relationship we've had different discussions along the many years of working with them. So it was a natural fit and the family and Smeal family are very excited to be partnering with us, as I think you saw by the Chairman of the Board's comment in our press release yesterday.

Rick, on the capital side?

Rick Sohm: Yes. I think, like we said, we're pretty comfortable with our capital structure. We've done a good job over the last year or so turning a lot of working capital into cash. We have plenty of liquidity.

I think we've said we're in the early stages of the turnaround, but we're happy that it's come along faster than we would have thought. And we really see this as an opportunity to accelerate the turnaround of the ER business. Daryl has laid out his five focal points for the Company, and the ER business returning back to profitability has been number one and continues to be.

So I think we're happy with the capital structure, adequate liquidity, and we'll continue to be opportunistic where it makes sense.

Ryan: Great. Thanks. One follow-up question on that and then I'll hop back in the queue. As you look at follow-on acquisitions, are you more focused on adding distribution, additional products, scale, et cetera? What are you kind of focused on? Or is it kind of all of the above? Thanks.

Daryl Adams: Yes, Ryan, this is Daryl again. Very good question. I think before we're ready to roll that out we want to make sure we've integrated this one properly, execute on it, get it behind us and then see what else might come our way.

But I think when you're in an industry that's consolidating, you have to be open to any opportunity that comes in front of you and be opportunistic. So, again, we're not going to be rigid, but the plan right now is to get it integrated, execute on it, and make sure that we make it accretive for 2017, like we expect.

Operator: Thank you. Ladies and gentlemen, at this time I am showing no further questions. So I'd like to turn the conference back over to Mr. Daryl Adams for any closing comments.

Juris Pagrabs: Thank you, Allison. This is Juris here. Thanks, everyone, for joining our conference call today to discuss the acquisition of Smeal Fire Apparatus. Have a safe and happy holiday, and we look forward to talking to you at the end of February, when we announce our fourth-quarter and full-year results. Thanks.

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