

The Shyft Group

Third Quarter 2023 Conference Call and Webcast

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CORPORATE PARTICIPANTS

Randy Wilson – *Vice President, Investor Relations and Treasury*

John Dunn – *President and Chief Executive Officer*

Daryl Adams – *President and Chief Executive Officer*

Jon Douyard – *Chief Financial Officer*

PRESENTATION

Operator

Good morning and welcome to the Shyft Group's Third Quarter 2023 Conference Call and Webcast. All participants will be in a listen-only mode until the question-and-answer session of the conference call. As a reminder, this call is being recorded.

I would now like to introduce Randy Wilson, Vice President, Investor Relations and Treasury of The Shyft Group. Mr. Wilson, you may proceed.

Randy Wilson

Thank you for joining this morning's call. As you may have already seen this morning, we issued a press release announcing the appointment of John Dunn as the Shyft Group's next President and Chief Executive Officer. He will succeed Daryl Adams, effective today, as part of our previously announced leadership transition plan. On today's call, I'm joined by Daryl Adams outgoing President and Chief Executive Officer, John Dunn; and Jon Douyard, Chief Financial Officer.

Before we begin, please turn to Slide 2 of the presentation, for our safe harbor statement. Today's conference call contains forward-looking statements, which are subject to risks that could cause actual results to be, materially, different from those expressed or implied.

Primary risks that management believes could materially affect our results are identified in our Forms 10-K and 10-Q filed with the SEC. We will be discussing non-GAAP information and performance measures, which we believe are useful in evaluating the company's operating performance.

For today's call, we've included a presentation deck that's been filed with the SEC and is also available on our website. We will provide a business update before moving on to a more detailed review of the results and our updated 2023 outlook. We will then open the line for Q&A.

Please turn to Slide 3, and I'll turn it over to Jon Douyard, who will lead today's prepared remarks.

Jon Douyard

Good morning and thank you for joining us to review our third quarter 2023 results. Overall, our team delivered third quarter performance that was in line with our expectations as our vocational and infrastructure related businesses continued to perform well, leading to another quarter of record profitability in specialty vehicles.

We remain focused on driving operational and commercial execution, as well as generating cash flow to enable long-term investment in the company.

For the third quarter, the company delivered solid operating cash flow of \$9.2 million, invested in the Blue Arc electric vehicle program and repurchased \$10.3 million in shares. In addition to our third quarter financial highlights, we were pleased to release our second Annual Sustainability Report highlighting the progress we've made on environmental, social and governance initiatives to benefit our team members, communities and other stakeholders.

In summary, we continue to make good progress on key strategic initiatives, and we are committed to driving improved execution in a challenging macro environment.

Turning to our market commentary on Slide 4, the long-term fundamentals for our key last mile delivery and infrastructure end markets remained strong. As we laid out in our July earnings call, the markets continue to be fluid, driven by higher dealer inventory levels in both last mile delivery and motorhome, as well as fleet strategy initiatives and mixed parcel volume reports that have limited recent order activity.

Throughout the third quarter, we were able to gain some clarity on these items, including the depth of OEM chassis production cuts, but additional items including the auto workers' strike that started in September continue to drive uncertainty across the market.

Fortunately, our infrastructure related truck businesses continue to see strong demand and the impact of the strike on those products has been minimal, to date.

We continue to stay close to our customers and monitor market drivers, while focusing on execution to ensure we respond appropriately, both commercially and operationally.

Turning to Slide 5, I will provide an update on our Blue Arc EV program and key milestones that relate to the product, production readiness and dealer network.

On our last earnings call, we discussed the field test that was in process with the large parcel customers.

We subsequently completed that test, and the feedback was, overwhelmingly, positive. The vehicle performance exceeded expectations and easily met the customers' daily needs, giving us confidence that our Blue Arc vehicle will meet the daily rigor demanded by our customers.

From a commercial perspective, we made further progress on building out our Blue Arc dealer network by adding Rush Enterprises, the operator of the largest commercial vehicle dealer network in North America.

In addition to Randy Marion, the dealer we announced in the fall of 2022, Rush expands our geographic reach and will be a fantastic representative of the Blue Arc brand.

As we communicated earlier in the quarter, we experienced an increase in quality issues related to production batteries from a key supplier. Our goal is and always has been to provide customers high quality products that will meet their daily needs and unfortunately, due to these battery issues, we have had to delay customer deliveries into 2024. We continue to work with the supplier to resolve these issues. Overall, customer interest remains high, and we are incredibly excited about our Blue Arc electric vehicle program.

Please turn to Slide 7, and I'll provide an overview of our third quarter 2023 financial results. We delivered earnings that were in line with our expectations, despite facing market pressures that impacted our year-over-year sales and margin performance. Sales for the third quarter were \$201.3 million, down 29.6% from the year ago quarter. Net income was \$4.5 million, or \$0.13 per share, compared to net income of \$17.3 million, or \$0.49 per share in the previous year.

Third quarter 2023 net income includes a tax benefit of \$2 million, primarily driven by favorable adjustments for R&D tax credits. In the third quarter, adjusted EBITDA was \$11 million, or 5.5% of sales, down from \$27.1 million or 9.5% of sales in the third quarter of 2022. These results include EV program spend of \$7.6 million, consistent with the prior year.

Excluding these expenses, adjusted EBITDA was 9.2% of sales. Adjusted net income was \$6.7 million, compared to \$18.6 million in the year ago quarter, while adjusted EPS decreased to \$0.19 per share from \$0.53 per share, last year.

I'll now walk you through our third quarter results by operating segment on Slide 8. In the quarter, Fleet Vehicles and Services achieved sales of \$124.3 million, down 32.6%, compared to \$184.5 million a year ago with strong truck body in aftermarket sales partially offsetting softness in walk-in van.

Adjusted EBITDA for the quarter was \$8 million versus \$24.4 million a year ago. Adjusted EBITDA margin was 6.4% of sales, compared to 13.2% in the third quarter last year.

Turning to specialty vehicles. Our team delivered another great quarter with record margin performance. Third quarter sales were \$76.6 million, a 26.3% decrease from \$103.9 million in the prior year driven by lower Motorhome market demand.

Adjusted EBITDA was \$16 million or 20.9% of sales, compared to \$15.6 million, or 15% of sales in the same period last year.

Please turn to Slide 9 for a 2023 outlook. Throughout the year, we remain cautious regarding our outlook as there was uncertainty across our key markets driven by broader economic headwinds.

Entering the third quarter, we expect uncertainty to remain given overall market conditions and, in the quarter, while we saw a sequential uptick in FBS orders, we continued to experience slower demand versus historical levels. We also gain further visibility to the severity of reduced OEM chassis supply for key parcel products and the OEM auto workers' strike began. The strike has been--impact has been minimal for us to-date, it has created uncertainty across the industry.

Given these factors, we have narrowed our 2023 outlook, notwithstanding further changes in the operating environment, as follows. Sales to be in the range of \$850 million to \$900 million, adjusted EBITDA of \$40 million to \$45 million. We expect positive operating cash flow for the year and additional working capital reductions in the fourth quarter, and we continue to take additional cost actions given the current environment and we'll manage the business aggressively, as we close out the year.

Please turn to the capital allocation update on Slide 10. Shyft's balance sheet remains a competitive advantage. In the third quarter, we generated \$9.2 million in operating cash flow, reflecting significant improvement over the prior year. The company's capital structure remains strong with a net leverage ratio of approximately one turn in a \$400 million revolver, which provides us solid access to capital.

We continue to fund organic growth initiatives focused primarily on Blue Arc EV and market expansion in our SV business. We maintain a healthy M&A pipeline and remain active in cultivating opportunities to accelerate growth.

In the quarter, we repurchased \$10.3 million of shares, as we believe the company represents an attractive value. We have now repurchased \$19.1 million of shares in 2023, leaving \$223 million remaining on our share repurchase authorization.

Please turn to Slide 11. The Shyft Group has a compelling industrial growth story with robust long-term market fundamentals. We are confident in our long-term strategy, the strength of our balance sheet, and we are focused on driving execution across the business.

Before turning the call over to Daryl and John Dunn for closing remarks, on behalf of the Shyft management team and all our team members, I would like to take the opportunity to thank Daryl for his vision, leadership and partnership, during his tenure with Spartan Motors and The Shyft Group.

While I was not here in 2024 when he started, I'm confident in saying that the company looks different and is much stronger today because of his leadership. He has left a great foundation for us as we move forward.

With that, I will turn the call to Daryl.

Daryl Adams

Thanks, Jon. Before we conclude today's call, I'd like to briefly take a moment to address the leadership news we announced this morning. Earlier this year in June, we announced a leadership transition plan, in which I will step down from my role as President and CEO, following the appointment of a successor.

Following a comprehensive search process in which the Board considered internal and external candidates, we have announced the appointment of John Dunn as Shyft's next CEO, effective today. John, previously served as President of Fleet Vehicle and Services business.

It's been a privilege for me to lead The Shyft team for the last nine years. I am proud of the incredible work our team has done to transform Shyft into an industrial leader in our attractive end markets, and last mile delivery and infrastructure.

As I look ahead, I'm confident Shyft is well positioned with a growing roster of innovative brands, strong prospects and we will work closely with John to ensure a seamless transition. Given John's familiarity with the company along with his significant leadership in manufacturing, operations and product development, we are confident John is the right person to lead Shyft through the next phase of transformation and growth.

And thank you to our analysts and the investment community for your interest and support of the company. I thoroughly enjoyed spending time with all of you and getting to know you, professionally and personally.

And I'll hand it over to John Dunn for some remarks.

John Dunn

Thank you, Daryl. I'm honored that the Board selected me for this role. With our great products, team members and customers, I'm excited to lead the organization in its next chapter of growth. In our fast-based industry, I recognize the need for Shyft to continually adapt and perform.

We will grow through innovation, commercial and operational excellence, product quality and an increased customer focus. We are committed to delivering shareholder value by allocating resources and efficiently deploying capital.

In early 2024, we will share more details regarding my business priorities and the company's strategic direction.

Thank you. And with that operator, we are now ready for the Q&A portion of the call.

QUESTION AND ANSWER

Operator

We will now begin the question-and-answer session. To ask a question, you may press “*”, then “1” on your touchtone phone. If you are using a speaker phone, please pick up your handset before pressing the keys. To withdraw from the question queue, please press “*”, then “2”.

The first question is from Matt Koranda of ROTH Capital. Please go ahead.

Matt Koranda

Hi guys, good morning and congrats to John and best of luck to Daryl. Just wanted to maybe dig into the FTS implied order flow that you reported, this morning. It does look like it's ticking up for the first time in several quarters and just wondered if you could maybe break down some of the factors that's driving demand in the quarter, specifically order flow like for truck body versus walk in van, and just the mix in the current order flow that you're observing?

Daryl Adams

Yeah, good morning, Matt. Yeah, I think we definitely saw an uptick in orders. I think as you know, our business is, historically, lumpy from an orders perspective. So, I wouldn't call one point a trend necessarily but it's positive to see some progress there. We continue to see activity on the truck body side of the business, as well as some of the opposite side of the business as well. I think walk-in van continues to be slow, which leads to some of the production cuts that we've talked about.

But I think we've also taken a number of actions, internally, under John's leadership within the FTS business. We brought in a new sales leader here in the quarter, which you may have seen on some of our social media and continue to look at different ways to attract the market. So, I think good progress, but again, we're not going to--we're not going to sit here and call it a trend at this point.

Matt Koranda

Okay, fair enough. And then just on Blue Arc. I mean maybe can we cover, one, I guess, are you getting any order indications? Obviously, you're indicating that the trials with customers have shown some success, but it doesn't seem like it's translated to order flow yet. What's holding it back, is that just essentially the fact that you have the battery issue and you won't be ramping production until 2024.

And then maybe also, if you could talk about the production ramp in '24, any additional thoughts when we should start modeling a ramp up in production in '24 for Blue Arc? And what's that mean in the context of the multi-year targets you guys put out last year around the ride and drive events?

John Dunn

Yeah, there's a lot to add to that question. But I mean, I think the battery issues are certainly a gating item at this point. We do talk about solid customer demand and interest. There's clearly Canadian demand. There's clearly other parcel demand that's out there that the customers have

a high level of interest that the dealers, whether it's Rush or Randy Marion that we've signed up to this point continue to react interact with some of the local customers.

And so, there continues to be that demand, but we obviously need to get through a battery issue before we let production go and move forward from that perspective.

So, as we look, when we announced the delay or the push out into 2024 in September related to that supplier issue, we didn't put a date on it because we continue to work through it, and so the team is very focused on driving closure to that and we continue to look at other opportunities and alternatives to mitigate that risk, as well.

So, I think from a long-term perspective, I guess point there is 2024, probably a little tough to model but I wouldn't--it's probably not early in the year at this point. But I think as you look out 2025 and beyond, we continue to make progress from a production standpoint and being able to address or react to the production curve and the demand profile.

And so, with the 2025 numbers, we still feel pretty confident and so we'll continue to provide updates to you on that. But we view this as more as a short-term issue than the longer term, a longer-term issue. And again, we're very confident in the product and the feedback that we've received from customers.

Matt Koranda

Okay. And then just to clarify, John, maybe, is the fix to the battery issue going to be a supplier change or is it going to be a fix with the existing supplier that you've that you currently have sourced from?

John Dunn

Well, I mean I think at the end of the day, we want to make sure that we have all options open, right. We've talked in the past about having multiple battery suppliers. We've announced one battery on the Class V on an ex-energy company as a better supplier on the Class V. And so we continue to look at options, but we're also engaged with our current supplier and trying to get resolution to the issue. And so, we're certainly not myopic in how we're trying to mitigate our resolve the problem here.

Matt Koranda

Okay. Got it. And then just one more on Blue Arc from me and then I'll leave it to others. But the agreement that you announced with Rush, maybe just a little bit more detail on how that works. Are they going to actually be taking any units into inventory, or is that essentially just they're agreeing to sell the product for customer order flow. Maybe just some additional color on sort of how that will function, once you get production up and running.

John Dunn

Yeah, I think it will be a combination of both. I think there'll be--they've got a fantastic footprint that covers really all of the country and a great service network. So, we'll have solid support from them as well from that perspective. But we would anticipate some level of stocking once we get into production.

I think we've talked in the past about how we're working with both the dealers on floor plan financing arrangements and those types of things. And so, we would expect it to operate in that normal commercial environment, but there's going to be opportunities where there is one-off orders that we end up leveraging our dealership network for, as well.

Daryl Adams

Thanks, Matt.

Matt Koranda

Okay. I appreciate it.

Operator

The next question is from Greg Lewis of BTIG. Please go ahead.

Greg Lewis

Yeah, thank you and good morning, everybody, and thanks for taking my questions.

Daryl Adams

Good morning.

Greg Lewis

Daryl, thanks for everything, congrats and maybe I'll see you on the circuit. Jon, I was hoping to get some more color around the guidance change as I kind of do the implied for Q4 and that is what it is. Is there any way to kind of parcel out realizing visibility is challenged, but is there any way to kind of think about the high-end and the low end and really, is that going to be around revenues, margins? Like any kind of more color as we kind of like trying to nail down that Q4?

Jon Douyard

Yeah, I mean, I think when we came out in July, we obviously had a pretty wide range. I think as we look at the quarter, some of the dynamics that we talked about in terms of chassis supply in the overall demand environment, I think some of the factors including the strike which, thankfully, made it seems to have made some progress last night, but there's a lot of variables.

So, the impact as we get closer to the end of the year from a volume perspective, I think we've got pretty good visibility, at this point. I mentioned in the prepared remarks that we continue to be aggressive from a cost standpoint. And so, we're continuing to sort of drive efficiency in the business, while managing the significantly lower volumes, year-over-year. So, the variability is probably more around the cost side and we're certainly pushing from a commercial perspective, as well.

Greg Lewis

Okay, great. And then just, I did want a little bit more color around the share repurchases, how we're thinking about that. Was that just opportunistic or is kind of we're here, this is something we're going to kind of look to continue to do and maybe it's not going to be continual given the outlook maybe for Q4. But kind of like any kind of broad thoughts about how you're thinking about the buyback here, just given where the stock is?

Jon Douyard

Yeah, I mean, I think, fortunately, we've got flexibility from that perspective. We've got a fantastic balance sheet, despite some of the challenging market environment, and so we were able to adapt and be flexible from that perspective.

I think we certainly feel there's value in the stock. Today, we bought close to 20 million shares, this year. We like the long-term prospects of the company. I think as we move forward, I think

we've got a significant authorization that's out there, but we also don't want to have that be the only capital allocation that we're doing as a company.

I think we'd like to be able to accelerate growth and we think organic and inorganic investments here, over time. And so, we'll continue to balance that as we look at it and I think in the quarter, it was an opportunity for us to repurchase shares that were above and beyond the annual dilution that we've done, over the last couple of years. So good opportunity, we'll continue to look at that as a lever for us given where our balance sheet strength is.

Operator

The next question is from Mike Shlisky of D.A. Davidson.

Mike Shlisky

Good morning, and thanks for taking my question. And Daryl, of course, thank you for your partnership over all these years. I really appreciate everything.

Daryl Adams

Thanks, Mike.

Mike Shlisky

Yes. So John, you just touched on it briefly in passing near your last answer, but it does look like Ford has essentially resolved the strike, overnight. I guess, do you feel materially better about your near-term prospects today compared to yesterday, especially regarding the Kentucky plant that was on strike? And do you have any feel for what the trust—will it get better coming out of Kentucky after the strike than we have before it?

Jon Douyard

Yeah, I mean I think the impact that we have seen to date has been relatively minimal. I think as we got closer to the end of the year and into 2024 is where we really would have seen some risks. And so, to the extent that the timing of this resolves itself in the next weeks or days, we certainly feel more confident as we enter 2024. There certainly may be some risk that we took into the narrowing of the guidance at the end of the year. But we haven't really seen an impact to date, or it was minor, anyway.

Mike Shlisky

Got it. I also wanted to touch on the battery issue, as well. Are there any costs that Shyft Group will have to incur that you had not foreseen, thanks to the issues that are going on with the supplier, or the cost to fix what's going on strictly going to be borne by that supplier.

John Dunn

Yeah, I think largely carried by the supplier. I mean, we obviously have a bit of a distraction internally in supporting that, which is inefficiency from a cost perspective. And then as we continue to look at other avenues of potential supply, I think there is—there could be some incremental costs from that perspective. But in terms of fixing this issue really lies in the supplier.

Mike Shlisky

One last one for me and that is the EBITDA and the SV Group. It was relatively flat despite I guess the RV business being down over the prior year. I'm just curious, is the RV business generally that challenged on EBITDA? We have a large decline, have no change in the segment EBITDA and is there anything you can do to fix that issue you're working on to get margins in the RV business to improve a bit?

John Dunn

Yeah, well, I think as you look at that business, I think with the volume declines that we've seen, you're certainly going to have some pressure just on Motorhome business in terms of margins and absorption. We don't have a ton of fixed costs tied up in that business but there's certainly still is some. And so, you know, we've, I think, structured that business appropriately for where the market is today.

I think when you look at the rest of the business, it continues to perform well. We continue to drive topline. We continue to increase capacity through pretty much the same footprint we've talked about before about expansion in Nashville.

These are all creating opportunities for us to gain share and drive the top line, which is--which is helping gain some leverage, but the team is also doing a fantastic job managing supply chain, managing the operations to push--to push margins. And so, we like that business. I think the service body infrastructure related businesses that we have in that portfolio, I think continue to perform really well. We like that space, and we'll continue to invest there.

Mike Shlisky

All right. Thanks so much, guys. I appreciate it.

Daryl Adams

Thanks Mike. Thank you.

John Dunn

Thanks Mike.

CONCLUSION**Operator**

This concludes our question-and-answer session. I would like to turn the conference back over to Randy Wilson for closing remarks.

Randy Wilson

Thank you, everyone. And we look forward to hosting investors at the Baird Global Industrials Conference in Chicago and the UBS Annual Industrial Summit in Florida. We thank you for your interest in The Shyft Group. And with that, Operator, please disconnect the call.

Operator

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