

# **Luxfer Holdings PLC (LXFR) Q1 2024 Earnings Call Transcript**

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**Body**

Luxfer Holdings PLC (LXFR)

Q1 2024 Earnings Conference Call

May 01, 2024 08:30 AM ET

Company Participants

Kevin Grant - Vice President, Investor Relations & Business Development

Andy Butcher - Chief Executive Officer

Steve Webster - Chief Financial Officer

Conference Call Participants

Steve Ferazani - Sidoti

Presentation

Operator

Good morning. My name is Shelby and I will be your conference operator today. Welcome to Luxfer's First Quarter 2024 Earnings Conference Call. [Operator Instructions]

Now, I will turn the call over to Kevin Grant, Vice President of Investor Relations and Business Development at Luxfer. Kevin, please go ahead.

Kevin Grant

Thank you, Shelby, and good morning, everyone. Welcome to Luxfer's first quarter 2024 earnings conference call. This morning, we'll be reviewing Luxfer's financial results for the first quarter ended March 31, 2024. I'm pleased to be joined today by Andy Butcher, our Chief Executive Officer; and Steve Webster, Chief Financial Officer.

Today's webcast is accompanied by a presentation that can be accessed at luxfer.com. Please note any references to non-GAAP financials are reconciled in the appendix of the presentation.

Before we begin, a friendly reminder that any forward-looking statements made about the company's expected financial results, are subject to future risks and uncertainties. We undertake no obligation to update any forward-looking statements, whether as a result of new information, future events or otherwise. Please refer to the safe harbor statement on slide 2 of today's presentation for further details.

During today's call, we'll be providing an adjusted first quarter 2024 financial results that exclude Graphic Arts based on our strategic review decision to divest that business.

Now, let me introduce Luxfer's CEO, Andy Butcher. Please turn to slide 3. Andy, please go ahead.

Andy Butcher

Thank you, Kevin, and good morning, everyone. Thank you for joining us. I'm pleased to report that Luxfer made good progress in the first quarter of 2024, increasing profitability and generating solid cash flow, despite variable demand in certain end markets.

The first quarter was slightly ahead of our internal expectations and reinforced our outlook for the remainder of 2024. I want to take a moment to commend and thank our dedicated team for their efforts that underpinned this result.

Sales came in at $83.1 million, reflecting some ongoing softness. However, we saw encouraging signs of recovery in some important areas, most notably for flameless ration heaters. In the quarter, we achieved an adjusted EBITDA of $10.5 million and reached adjusted earnings per share of $0.20.

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This represents a significant improvement over the last quarter of 2023, driven primarily by enhanced profitability in our Elektron segment. Additionally, we delivered $3.6 million of operating cash, holding our lower levels of net debt, resulting in reduced interest payments and maintaining our low leverage.

These overall results reflect the effectiveness of our recent operational adjustments. We have maintained our service to our customers, restructured our manufacturing footprint, and ensured rigorous control over expenses. At the same time, we've initiated the sale of Graphic Arts while also collecting a first significant legal repayment from our insurance company.

So, a good start to the year. I look forward to sharing more details over the next few minutes. Let's first move to slide 4 for an update on our comprehensive strategic review. In October, we accelerated and expanded our annual strategic review to enhance business performance and unlock shareholder value.

As you may recall, this effort produced three important conclusions. First, we initiated the sale of our Graphic Arts business. We retained XMS Capital Partners to advise on the sale. The process is well underway with significant engagement from potential buyers. We are targeting closing a transaction by year-end.

Second, we continue to optimize costs and invest in our Gas Cylinders and Elektron businesses, enhancing their competitive positioning to provide attractive growth and returns. Elektron is starting to show a promising demand recovery benefiting also from our efforts to lower costs.

Gas Cylinders will continue to capitalize on growth in alternative fuel products, which we expect to begin accelerating in the near to intermediate term. As a result, we remain optimistic about the sustainable profitable growth prospects for both businesses in 2025 and beyond.

And third, as previously communicated, we concluded that our Gas Cylinders and Elektron segments operate with minimal strategic synergies. So, as we drive improved financial outcomes in both businesses, we will continuously monitor both business performance and market conditions to maintain full optionality to maximize shareholder value.

Now turning to Slide 5. Let me update you in more detail on the impact of the actions we've taken to enhance our performance in 2024. The first quarter results were encouraging with significant margin expansion in our Elektron business, supported by our footprint simplification and a reduction in fixed costs.

These moves not only enhanced profitability, but have also positioned us for the anticipated uplift in demand for military flare powders which, is now materializing. Also in Elektron, our leading Flameless Ration Heater technology continues to establish Luxfer as the supplier of choice for food packages and assemblers.

The Defense Logistics Agency's 2024 award is in line with prior year, confirming our critical role in the production of Meals Ready-to-Eat and contributing to our improved first quarter sales. During our last call, I announced our renewed multiyear supply agreements with key SCBA customers.

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Today I'd like to mention our collaboration with one of those customers, in supplying the U.S. Air Force with our Super Light Cylinders which is ongoing through the first half of this year. This partnership demonstrates our commitment to providing top-tier safety equipment as well as our dedication to ensuring our servicemen and women have access to the most advanced reliable technology.

Our initiatives in Clean Energy have included refining the footprint of our North American alternative fuel operations now complete and the construction of our bulk gas transportation module facility in the U.K. The latter effort is pivotal for our future growth.

And I was pleased to participate in discussions with two potential module customers last month. Both are keen on leveraging our innovative products for transportation and their excitement reaffirms the potential for near-term growth in this arena.

Additionally, we are making promising strides in product development, assisted by a recent Clean Technology grant, awarded by Alberta Innovates in Canada. This funding not only accelerates our development of our Cutting-Edge Type 4 Hydrogen Cylinder, but also symbolizes another step forward in our commitment to Energy Solutions.

And finally, we have received an initial insurance recovery payment, recouping approximately $1.3 million of our historical legal costs. We are continuing to make strong efforts to reclaim other prior legal expenses and I look forward to updating you on our progress.

In conclusion, our strategic decisions are driving improved profitability and strong cash generation. We are on our way to achieving profitability levels, that reflect the value that our innovative engineering brings to our customers and our industries.

At this time, I'll turn the call over to Steve, to discuss our Q1 results in greater detail, explain our improved profitability from the prior quarter and update on the 2024 outlook. Steve?

Steve Webster

Thanks, Andy and good morning everyone. I'd like to start this morning by reviewing our consolidated financial results and bridges for the first quarter 2024. Please note that the non-GAAP measure numbers I refer to are on an adjusted basis excluding the Graphic Arts business.

Let's turn to Slide 6. Looking at the top of the slide, while our sales of $83.1 million reflect an 11.5% decrease from the prior year, it's important to highlight the considerable profitability improvements seen since the previous quarter.

Adjusted EBITDA for the first quarter was $10.5 million with margins at 12.6%, comparing favorably to the $8 million and 9.1% in the prior quarter. Additionally, our adjusted earnings per share rose to $0.20 from $0.13 in the third -- fourth quarter underlining the improvements in our profitability.

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Shifting to our balance sheet and our cash flow dynamics, cash flow from operations was solid, generating $3.6 million and our free cash flow reached $2.2 million significantly improved from the seasonal outflow we experienced in the first quarter of the previous year. And we have maintained strong liquidity ending the quarter with net debt of $71.6 million and a leverage ratio of 1.7 times.

Looking at the sales bridge, our revenue of $83.1 million compared to $93.9 million in the prior year. We saw a favorable impact from pricing adjustments contributing an additional $1.6 million alongside a $0.6 million benefit from foreign exchange. However, these gains were offset by a $13 million decrease in volume with tough prior year comps in the general industrial and the military flare markets.

Turning to the adjusted EBITDA bridge. Our first quarter adjusted EBITDA was $10.5 million, down $1.5 million from the previous year, with the impact of adverse volumes partially offset by some cost deflation, incremental price in cylinders, considerably lower legal costs and favorable manufacturing efficiencies in Elektron. Despite the ongoing macro challenges, our adjusted EBITDA margin came in at 12.6% this quarter, only slightly down from last year's 12.8% and confirming our prior projections of a Q1 rebound.

Please turn to slide 7 for a detailed review of Elektron's first quarter financial results. Elektron's first quarter of 2024 exhibited a strong turnaround in profitability despite the year-over-year sales decline. We saw significant sequential improvement with an 840 basis point increase in gross margin and a substantial rise in adjusted EBITDA margin to 17% from 4.4%. This positive shift was driven by anticipated volume recovery, enhanced manufacturing efficiencies and the streamlining of our cost structure through ongoing initiatives.

Despite lower sales across all segments compared to a busy Q1 2023, we are seeing pockets of recovery notably in flameless ration heaters within our defense, first response and healthcare market. However, broader declines were noted in this end markets due to decreased military flare magnesium powder sales following customer destocking.

The Transportation segment was also lower, primarily due to softer demand for auto catalysis materials. Finally, the general industrial market declined modestly this quarter compared to prior year but demonstrated significant sequential improvement over quarter four. All that said, given Elektron's weaker performance in the second half of last year, we are very encouraged by the significant recovery in margins as we start this year.

Now please turn to slide 8 for a detailed review of the Gas Cylinders' first quarter financial results. Gas Cylinders are seeing positive momentum, particularly in the firefighter self-contained breathing apparatus market, enhanced by renewed long-term contracts which have lifted our margins towards historic norms.

In the quarter, sales rose to $45.4 million, up 9.4% year-over-year and achieved a notable gross margin improvement of 450 basis points, reaching 17%. Our adjusted EBITDA margin increased by 300 basis points to 9%.

In our market segments, Defense, First Response and Healthcare sales increased over the previous year, thanks to continued demand for lightweight SCBA and medical cylinders. Transportation sales also grew with stronger demand for alternative fuels products. Meanwhile, the general industrial end market still encounters headwinds the sales decline this quarter although this continues to represent a relatively small part of the Gas Cylinders business.

We are encouraged by the operational achievements demonstrated this quarter. As we capitalize on our strengths and technical know-how, Gas Cylinders remains committed to driving value and excellence for our stakeholders and customers.

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Now please turn to slide 9 for an update on our full year 2024 financial guidance. As a reminder, our 2024 guidance does not include the Graphic Arts business. Our financial outlook has been raised to reflect the better than expected improvements in the first quarter and the recent recovery of historical legal fees.

While sales do remain a challenge, we are now projecting adjusted EBITDA to be between $44 million and $48 million with adjusted diluted EPS ranging from $0.75 to $0.90 and with free cash flow anticipated to be between $21 million and $25 million.

We continue to emphasize maintaining a robust balance sheet and enhancing our free cash flow. This strategy supports a dual approach to capital management allowing for continued investment in growth opportunities while also returning capital to shareholders through steady dividends and share repurchases.

In summary, I'm genuinely excited about the recent uptick in performance of Elektron, the sustainable improvement in Gas Cylinders margins and the robust cash conversion rates we've achieved. This collective result underscores our strong position and readiness to embrace future opportunities.

Now, I'd like to turn the call back to Andy. Andy?

Andy Butcher

Thanks, Steve. I will conclude my prepared remarks, on Slide 10. As we progress through 2024, I'm pleased to see that we are on the right track. The latter half of 2023 presented various challenges, and there is a long road ahead, but the outlook for 2024 is promising, bolstered by both improvements in end-market demand and our operational performance.

As we conclude this update, I'd like to highlight the significant progress we have made over the last few months, that maintains my confidence in our long-term success. We have secured multiyear supply agreements with key SCBA customers, incorporating our supply to the U.S. Air Force of Super Light Cylinders.

We are capitalizing on early signs of demand recovery within certain Elektron Industrial and Defense sectors, we have streamlined our North American alternative fuel operations and constructed a new capability in Nottingham UK, enhancing our role in the Green Energy transition.

We have addressed our insurance coverage issues and have recently started to recover some of the historical fees. And we have carefully managed our working capital, which has improved our free cash flow and maintained our low net debt, driving lower capital charges and providing resilience and future optionality.

I am encouraged by our progress, and cautiously optimistic about the rest of 2024. Despite the current industrial market environments, we are seeing a recovery in demand for Elektron applications and strong performance in our Gas Cylinder segments.

Luxfer's long-term strategy remains focused on leveraging our materials engineering expertise to solve customer challenges, improve profitability and generate strong cash flows. We are making significant progress in our initiatives to unlock shareholder value and are confident in our ability to achieve enhanced margins and sustained earnings growth.

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With that, I'd like to turn the call back to the operator, for the Q&A session. Shelby, please go ahead.

Question-and-Answer Session

Operator

[Operator Instructions] And we'll take our first question from Steve Ferazani with Sidoti. Your line is open.

Steve Ferazani

Good morning, Andy. Good morning, Steve. Obviously really surprised and impressed with the sequential margin improvement in Elektron. It was coming a lot faster than we suspected not sure how much faster it was on your side.

You provided a lot of color on the call but if you could add a little bit of detail on where you were seeing it and the ability to generate further margin improvement given what we expect to be some deflationary impact on raw material costs from raw material costs?

Andy Butcher

Yeah. Thank you, Steve and thanks for joining the call. Yes, we are pleased with our Q1 results. And they were a little ahead even of internal expectations. So that was good. On the sales side, we were especially pleased to be able to deliver on the higher level of sales of Flameless Ration Heaters.

That was something we projected, but it was very, very pleasing that the award from the Defense Logistics Agency came in at the normal levels as we had expected. So we saw a strong rebound from Q4 on that very important product line. I'll perhaps ask Steve, to make a couple of extra comments on margins.

Steve Webster

Yeah. I mean, I think, certainly the majority of the margin improvement was in -- or the majority of the margin improvement was in Elektron. And if you look at that there's three main areas. One of them is volume and mix.

I mean the FRH sales are one of our better margin products. So that contributed roughly 1/3 I'd say the margin improvement.

I talked about manufacturing efficiencies and also some cost savings from some of the projects we've done. That's probably about another third. And then, finally the significant lower legal cost is the remaining third. So three buckets there, volume and mix manufacturing efficiencies cost savings and then lower legal costs.

Steve Ferazani

Given how much improved so the sustainability upside and any reason why you wouldn't raise guidance more given the early strength in that margin recovery on Elektron?

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Andy Butcher

Yes. Thanks for that. This is Andy here again. Look let me start by underscoring that I am encouraged Steve by the recent developments that we've seen especially in Elektron. And we do approach the remainder of 2024 with some cautious optimism despite ongoing uncertainties in the industrial macro environment.

We have witnessed the expected recovery in demand across certain Elektron applications. And we're pleased with the robust performance in our Gas Cylinder segment. It does increase our confidence in the annual guidance we provided and we are pleased to have been able to uplift the guidance. That's a mix I think of the improved performance we've delivered and those legal fee recoveries.

Steve Ferazani

Any update on timing of the bulk gas facility? And can you provide a little bit of detail on I think what you noted was some strength in the North American CNG market?

Andy Butcher

Yes. Yes. Great. First of all on hydrogen of course and bulk gas of course the hydrogen economy needs infrastructure to move hydrogen from where it's produced maybe a remote wind farm to where it's used in a city or industrial center. And containers of multi-element gas containers are the preferred solution. So with our lightweight cylinder technology we've developed these range of containers. The development of the facility is going well and we do expect that we'll make the first sales from our Nottingham, UK facility later this year with the opportunity then for a rapid growth in 2025.

On the CNG side compressed natural gas CNG North American demand remains high. Sales of our lightweight high capacity Type four cylinders doubled to almost $8 million in the quarter compared to prior year. It's been a pretty exciting start to the year there and we expect that to continue particularly highlight the upcoming tailwinds from the new X15 Cummins CNG engine that's being introduced throughout the summer and should give us some additional momentum there as we move towards the end of the year and into 2025. So, yes, quite excited Steve about both gas and CNG.

Steve Ferazani

Great. Thanks, Andy. Thanks, Steve.

Andy Butcher

Thanks, Steve.

Operator

There are no more questions in the queue. At this time, I'll turn the call over to CEO, Andy Butcher for final remarks.

Andy Butcher

Thank you for your question, Steve and thanks to everyone for joining the Luxfer call. Today, we've covered vital areas. Our strategic commercial developments are setting a strong pace. We're seeing an initial recovery in market demand. Our operational consolidations are enhancing efficiencies. We've successfully started to recover historic legal fees and our financial health continues to strengthen. Each of these points is a testament to our resilience and our determined approach to improving our business.

As always, thank you for your interest and support in Luxfer. We look forward to updating you on our progress next quarter.

Operator

This concludes Luxfer's Q1 2024 earnings call. A recording of this conference call will be available in about two hours. A link to a recording of this webcast will be available on the Luxfer website at www.luxfer.com .

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