

# **Matthews International Corporation (MATW) Q3 2024 Earnings Call Transcript**

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**Body**

Matthews International Corporation (MATW)

Q3 2024 Earnings Conference Call

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Company Participants

Bill Wilson - Senior Director-Corporate Development

Joe Bartolacci - President and CEO

Steve Nicola - CFO

Conference Call Participants

Daniel Moore - CJS Securities

Justin Bergner - Gabelli

Presentation

Operator

Greetings, and welcome to Matthews International Third Quarter Fiscal 2024 Financial Results Conference Call. At this time all participants are in a listen-only mode. A brief question-and-answer session will follow the formal presentation. [Operator instructions] As a reminder, this conference is being recorded.

It is now my pleasure to introduce your host, Mr. Bill Wilson, Senior Director, Corporate Development. Thank you. Mr. Wilson, you may begin.

Bill Wilson

Thank you Ranchu, and good morning, everyone. And welcome to the Matthews International Third Quarter Fiscal Year 2024 Conference Call. This is Bill Wilson, Senior Director of Corporate Development. With me today are Joe Bartolacci, President and Chief Executive Officer; and Steve Nicola, our Chief Financial Officer.

Before we start, I'd like to remind you that our earnings release was posted on our website, www.matw.com , in the Investors section last night. The presentation for our call can also be accessed in the Investors section of the website under Presentations. Any forward-looking statements in connection with this discussion are being made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Factors that could cause the company's results to differ from those discussed today are set forth in the company's Annual Report on Form 10-K and other public filings with the SEC.

In addition, we will be discussing non-GAAP financial metrics and encourage you to read our disclosures and reconciliation tables carefully as you consider these metrics. In connection with any forward-looking statements and non-GAAP financial information, please read the disclaimer included in today's presentation materials located on our website. And now I'll turn the call over to Joe.

Joe Bartolacci

Thank you Bill. Good morning. Despite encountering challenges in our Industrial Technologies segment, we were pleased with the results of the remainder of our businesses. Consolidated sales and adjusted EBITDA declined on a year-over-year basis primarily due to ongoing customer delays of shipments and installations for our energy storage products. Also, slow market conditions in the warehouse automation business continued during the quarter and represented a smaller part of the overall decline in our Industrial Technologies segment.

Our Memorialization segment reported another solid quarter on a year-over-year basis especially when you consider that the US casketed deaths declined mid-single digits during the quarter. Although memorial and casket volumes were down, improved pricing and mausoleum sales offset much of the decline. Also, a small acquisition completed earlier in fiscal '24 contributed favorably to the segment's results. Although it is early, we saw improved volumes and good product mix through the month of July, which should allow the business to finish the year strong. As stated in the past, this segment has normalized post-COVID at a performance which is significantly higher than pre-COVID.

SGK continued to demonstrate stable top-line growth with another good quarterly performance, benefiting from continued improvements in the pricing environment and cost reduction actions. SGK's growth also drew from a more buoyant private label market and increased activity in the European packaging market, a welcome sign which we hope will continue. SGK has won several significant new accounts over the last several quarters, driven by greater market differentiation through automation and technological solutions, which have begun to implement -- which we have begun to implement and which are being well-received by our clients.

Assuming market conditions remain consistent, this position is positioned for continued improvement in fiscal 2025. Additionally, our e-commerce digital initiative continues to deliver positive results, and we expect to exceed the $40 million sales target we set earlier in the fiscal year. This represents an area of focus and opportunity for us as our clients are looking for ways to consolidate their e-commerce marketing spend, and we are well positioned to cost-effectively deliver that solution.

With respect to our Industrial Technologies segment, total sales were lower for the quarter, primarily driven by continued customer delays of shipments and installations of energy storage equipment. It's important to note that the particularly strong quarter that was reported last year resulting from the nature and timing of the revenue reported last year. The higher margin revenue recognized last year reflected the high-value portion of the energy storage order announced last year.

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The higher margin is attributable to the proprietary nature of our engineered solution which was predominantly design and engineering services last year. The timing and nature of last year's revenue recognition makes for a more difficult comparison this year. Third quarter warehouse automation results were down consistent with industry trends. End-users continue to delay placing orders, as confirmed by industry data and likely related to the higher interest rate environment.

With that said, we do see quoting activity picking up and believe that we have hit the bottom of this slowdown as indication of the recovery begin to appear. Product Identification revenues for the third quarter were flat year-over-year, though we're expecting a strong finish to the year. Consistent with our focus on constant innovation, we're expanding our portfolio in this business with the launch of a new line of laser products in August. The launch of our laser system is designed for marking and coding on consumer packaged goods, and together with our new print head technology, we will further develop our strategy of attacking this $2 billion market opportunity with innovative superior solutions.

Regarding our new printhead technology, we are still on track for our launch in early next year. Our strategy is to continue to develop on this new and disruptive solution which expands the market opportunities to areas which we currently do not serve. With respect to our energy business, as I'm sure you are aware, Tesla recently filed a suit attempting to restrict us from selling our dry battery electrode equipment solutions to other companies and alleging that we have misappropriated unidentified trade secrets resulting in significant damages.

Our position with respect to the lawsuit remains clear, firm and unchanged. This is an effort by Tesla to bully us and force us to transfer our highly valuable proprietary technology to them by undue pressure. We have been offering various engineered solutions in the battery industry since 1998 for some of the largest companies in the world. We produced the first dry battery electrode equipment and converted lithium-rich powder to film and applied it to aluminum and copper foils to produce the first dry battery electrode before ever having any discussions, let alone orders from Tesla. Tesla sought us out due to our well-established industry-leading knowledge.

Our technology provides battery producers significant reductions in capital and operating expenses and our multi-year head start makes us the go-to company when it comes to the equipment needed to produce dry battery electrodes. This is a capability that we have developed, marketed and commercialized for over 25 years through relationships with some of the earliest innovators in battery development.

During that time, we have accumulated extensive know-how and IP on battery equipment in general and in particular, dry battery electrode equipment, which has led to the groundbreaking energy storage capabilities. Thus, we remain confident we will prevail in this meritless lawsuit and the entire global industry will benefit from our tremendously valuable technology.

As for the impact of the lawsuit on our business, legal fees are having an impact on our SG&A cost. But as stated earlier, we continue to draw industry-wide interest in our technology. We continue to take orders for DBE equipment and production lines from the largest global battery manufacturers and automotive OEMs. We are extremely confident in the company's ongoing ability to produce and sell DBE manufacturing equipment, and we continue to make significant advancements in the technology, improving its efficacy and its speed.

Many have asked how did we get into this business? It was not an accident. Our intellectual property is built on a platform of innovation especially in the case of our energy business. For years, we have taken activities done in batches such as stamping or pressing and designed equipment to perform these actions and continuous process using roles or calendaring equipment. These highly engineered calendars play a critical role in the DBE process.

One final piece of clean energy news as further evidence of our roll-to-roll process know-how, we were recently awarded the Department of Energy Cooperative Agreement together with General Motors, NeoGraf Solutions and others for the development of hydrogen fuel cells. The grant is to fund advancements in the production of fuel cell stacks with inexpensive graphite bipolar plates that will materially reduce the cost of fuel cells. Our hydrogen market is still in its infancy, but as we have done in the past, we are at the forefront of this developing technology and we are operating with some of the leading companies in the world.

Finally in our earnings release, we mentioned plans to initiate a cost reduction program in the fourth quarter spanning several of our business units, as well as our corporate function. We are targeting up to $50 million in annual cost savings with the bulk to be driven by changes in our engineering and tooling operations in Europe. You may recall that after announcing the acquisition of OLBRICH in the fourth quarter of fiscal '22, we communicated our intention to extract savings once an agreement was reached with OLBRICH Union in Germany. We believe this is the right time to take this action and that it positions our business to capitalize on future growth opportunities while making OLBRICH, a significant contributor to our overall portfolio.

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In addition, a significant portion of the savings comes from the reduction of corporate overhead resulting from years of planning and implementation of a global business services function, which capitalizes on our SAP backbone. These actions are expected to span the next two fiscal years, but the majority of the cost savings will be achieved next year. With respect to our balance sheet, as we have outlined at the beginning of the fiscal year, we are laser focused on reducing our outstanding debt. With that in mind, through another quarter of good cash flow management, we reduced our debt by $13 million and planned further reductions through year-end.

Additionally, we are on track to refinance our outstanding bonds by fiscal year-end. As we approach fiscal year-end we expect energy storage shipments and installation in orders for warehouse automation to pick up in the fourth quarter and into fiscal '25. Memorialization in SGK should be in-line with last year's results and provide a solid foundation for growth. As a result, we project adjusted EBITDA for fiscal 2024 to be in the range of $205 million to $210 million.

I will now turn the call over to Steve for more insight on our financial results.

Steve Nicola

Thank you, Joe. Good morning. Let's begin with Slide 7. For the fiscal 2024 third quarter, net income attributable to the company was $1.8 million or $0.06 per share compared to $8.7 million or $0.28 per share a year ago. On a non-GAAP adjusted basis, earnings for the current quarter were $0.56 per share compared to $0.74 per share last year. The impacts of lower consolidated adjusted EBITDA and higher interest expense were partially offset by income tax benefits for the current quarter.

Consolidated sales for the fiscal 2024 third quarter were $427.8 million compared to $471.9 million a year ago. Our largest businesses, Memorialization and SGK Brand Solutions continued to perform relatively well for the quarter as the consolidated sales decrease primarily reflected a decline for the Industrial Technologies segment. Sales for the SGK Brand Solutions segment were modestly higher than a year ago, primarily reflecting increased sales for the European packaging business and in the private label market.

Sales for the Memorialization segment for the current quarter remained relatively steady compared to a year ago reporting only a modest decline despite lower unit volumes related to a decrease in US casketed deaths. The decline for the Industrial Technologies segment primarily reflected lower sales for its engineering and warehouse automation businesses.

Consolidated adjusted EBITDA for the fiscal 2024 third quarter was $44.7 million compared to $56.2 million a year ago. The decrease mainly resulted from a decline in the Industrial Technologies segment, primarily related to its engineering and warehouse automation businesses. Adjusted EBITDA for the Memorialization and SGK Brand Solutions segments were only modestly lower for the quarter, which were substantially offset by lower corporate and non-operating costs.

Please see the reconciliations of adjusted EBITDA and non-GAAP adjusted earnings per share provided in our earnings release. And please move to Slide 8 to review our segment results. Sales for the Memorialization segment for the fiscal 2024 third quarter were $202.7 million compared to $208.7 million for the same quarter a year ago. Sales volumes for cemetery memorials, caskets and cremation equipment were lower for the quarter compared to last year as US casketed deaths declined. These declines were significantly offset by the favorable impacts of improved price realization and higher mausoleum sales. Recent acquisitions also contributed to the segment sales for the current quarter.

Memorialization segment adjusted EBITDA for the current quarter was $38.7 million compared to $39.9 million for the same quarter last year. The decrease primarily resulted from the impact of lower sales volumes and increased labor and material costs. These declines were substantially offset by the favorable impacts of improved pricing and benefits from cost-savings initiatives.

Please move to Slide 9. Sales for the SGK Brand Solutions segment increased to $33.4 million for the quarter ended June 30, 2024 compared to $132.6 million a year ago. The increase primarily reflected higher sales in the private label market and for the segment's European packaging business, and improved price realization to mitigate inflationary cost increases.

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Currency rates had an unfavorable impact of $2.6 million on current quarter sales compared to a year ago. Adjusted EBITDA for the SGK Brand Solutions segment was $16.1 million for the current quarter, which was relatively consistent with the segment's adjusted EBITDA of $16.4 million a year ago. The benefits of higher sales and the segment's cost reduction actions were offset by higher labor related costs and performance based compensation. The segment's year-to-date adjusted EBITDA increased 12% to $44.3 million for the current year compared to $39.6 million last year primarily reflecting the benefits of their cost reduction actions.

Please move to Slide 10. Sales for the Industrial Technologies segment for the fiscal 2024 third quarter were $91.7 million compared to $130.5 million a year ago. The decrease primarily resulted from lower sales for the segment's engineering and warehouse automation businesses. As we previously discussed, our engineering sales have been unfavorably affected by customer delays in shipments and installations. Additionally, operating results for our warehouse automation business have been unfavorably impacted by the current slow conditions in the US warehouse industry.

However, we are starting to see signs of improvement based on recent quoting rates. In addition, recent divestitures contributed to this segment sales decline. Changes in foreign currency rates also had an unfavorable impact of $1.4 million on the segment's current quarter sales compared to a year ago. Adjusted EBITDA for the Industrial Technologies segment for the current quarter was $4.2 million compared to $15 million a year ago. The decrease primarily reflected the impacts of the sales declines in the engineering and warehouse automation businesses.

The declines were partially offset by lower performance based compensation and the benefits of operational savings initiatives. Changes in currency exchange rates had an unfavorable impact of $217,000 on the segment's current quarter adjusted EBITDA compared to a year ago.

Please move to Slide 11. Cash flow from operating activities for the quarter ended June 30, 2024, was $13.5 million compared to $32.2 million a year ago. Relative to a year ago, cash flow for the current quarter primarily reflected the company's lower consolidated adjusted EBITDA, offset partially by the benefit of working capital reductions.

Outstanding debt was $830 million at June 30, 2024, compared to $843 million at the end of last quarter, representing a reduction of $12.6 million during the third quarter. Net debt which represents outstanding debt less cash, was $787 million at June 30, 2024 compared to $797 million at March 31, 2024 representing a reduction of $9.8 million during the third quarter. Since the beginning of calendar 2024, the company has reduced its outstanding debt and net debt balances by $32 million and $37 million respectively.

At June 30, 2024, the company's leverage ratio based on net debt and trailing 12-months adjusted EBITDA was 3.77%. As we reported last quarter, we renewed our $750 million domestic revolving credit facility during the fiscal 2024 second quarter and are now focused on refinancing our bonds which do not mature until December 2025. We currently expect this refinancing to be completed before the end of this fiscal year.

For the fiscal 2024 third quarter, the company purchased only approximately 115,000 shares under a stock repurchase program, as we remain primarily focused on debt reduction. Approximately 30.6 million shares were outstanding at June 30, 2024. As Joe just noted we are initiating cost reduction programs beginning this quarter that will span several of our business units and corporate functions.

We are targeting annual consolidated savings from these programs to be up to $50 million, with the most significant portion from our engineering and tooling operations in Europe. Finally, the Board last week declared a quarterly dividend of $0.24 per share on the company's common stock. The dividend is payable August 19, 2024 to stockholders of record August 5, 2024. This concludes the financial review, and we will now open the call for any questions.

Question-and-Answer Session

Operator

Thank you. We will now be conducting a question-and-answer session. [Operator instructions] The first question comes from the line of Daniel Moore with CJS Securities. Please go ahead.

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Daniel Moore

Thank you. Good morning Joe. Good morning Steve. Thanks for taking my questions.

Joe Bartolacci

Good morning Dan.

Daniel Moore

Start with the guide and then kind of maybe switch gears to energy storage. The revised guidance for fiscal '24 in terms of the implication for Q4, how much energy storage revenue is in there and just talk about your confidence and any risk that maybe some of that additional revenue or shipments might slip into fiscal '25?

Joe Bartolacci

So, I mean let me kind of parse that out for you, Dan. We expect to carry over somewhere of about $60 million to $70 million worth of backlog in the energy business into 2025. Our current expectation is we should have about $30 million or so of billings in the month -- in the quarter that we are approaching right on the fourth quarter. So our expectations and we have had a pretty good discussion in terms of that with our customer and right now, that is the current plans that will ship through late February of next year with some trailing orders to be delivered thereafter.

Daniel Moore

That's helpful. And then I think you said in the prepared remarks you expect energy storage orders to pick up in Q4 and into fiscal 2025. I don't know if that was orders was for --.

Joe Bartolacci

It was revenue recognition. Warehouse and product identification is what we are seeing things start to pick up again.

Daniel Moore

Got it. That is really helpful. Sticking there on the DBE front you talked about plans to build battery production capability in-house and I think you said spending an incremental $40 million over the next 12 plus months. Are those plans still on track? And what would that look like from a capacity perspective once that build-out is complete?

Joe Bartolacci

So let me explain exactly what that is. First off the number is materially lower as a result of some of the cost structures initiatives that we've initiated. We are freeing up a fair amount of real estate to be able to house it, so the capital cost will come down materially. Secondly, we are not building production capability as much as we are building a production line. That production line, it will allow an accelerated adoption of the DBE solution by some of the largest customers in the world.

So, we are moving away from selling a lab machine and then a small prototype machine, and then finally waiting for an order. This is the process of standardizing the production line to a methodology that is consistent and we can sell repeatedly. That will benefit time-line for adoption significantly with some of the largest customers as they try to go up from where they are today. But more importantly, it should improve our cost structure as we standardize around a definitive solution.

Daniel Moore

Really helpful. One more on energy storage, and then I will ask one more and jump back in queue. I know you are too early to get into fiscal '25 guidance but given kind of where we are in terms of orders right now, do we think about '25, as being a growth year in that business? Or could that inflection maybe push out to fiscal 2026?

Joe Bartolacci

I would tell you that 2025 is going to be a good year, not a -- right now, things can change so dramatically so quickly, Dan. But I would not expect a significant growth year I would expect a good year in that business. The cost structure initiatives we are taking over there will make the overall engineering solution better. We are taking out a significant amount of costs over there. But more importantly, I'm hoping 2025 to be -- once we get past the litigation, to be more of an announcement year where we can speak more freely about what we are doing.

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Daniel Moore

That is really helpful. Last for me. You mentioned green shoots or maybe my word not yours, on warehouse automation, maybe all the quoting rates any additional color you can give there around what you are seeing and hearing from customers and when we might see a little bit of return in that business. Thanks again.

Joe Bartolacci

I'm hoping to have -- I mean, unfortunately, some -- we're working with some of the largest players in the industry Dan, when it comes to e-commerce and store fulfillment. And the names, unfortunately, are not allowing us to use their names, but I can tell you they are national brands in every sense. Those orders are in pipeline right now. I'd say, that they are in final negotiations, fairly significant orders, but interests are -- it has increased significantly around finally moving forward.

Unfortunately, as you know, this is a cyclical business when it comes to the year. Generally, we are out of warehouses in the first quarter, so don't expect a big first quarter as much as you start to see those revenues into the second and third quarter of next year.

Daniel Moore

Understood all. I'll jump back if any follow-up. Thanks Joe.

Operator

Thank you. Next question comes from the line of Justin Bergner with Gabelli Funds. Please go ahead.

Justin Bergner

Good morning Joe. Good morning Steve.

Joe Bartolacci

Hi, Justin.

Justin Bergner

A few questions here. Just to make sure the onetime cost to achieve the savings and the $50 million cost out plan of $40 million, those are all cash?

Joe Bartolacci

No, not all.

Steve Nicola

No, the majority of them are cash, Justin. But there is a component of it that would be asset write-off related.

Justin Bergner

Okay. Any quantification of the cash portion?

Steve Nicola

No, I don't have those numbers with me.

Joe Bartolacci

We can get that for you, Justin.

Justin Bergner

All right. And then depending upon how the situation resolves itself with Tesla, I mean, could you see yourselves downsizing that cost takeout program not just centered around Europe?

Joe Bartolacci

Let's put it this way. As it relates to OLBRICH itself, now as it relates to the rest of our engineering business over there perhaps. I mean, the reality is that we're positioning it for growth over there so the cost that we are taking out were anticipated when we acquired OLBRICH. If you recall, OLBRICH was a business we paid EUR45 million for that -- what is coming out of bankruptcy for all practical purposes, and it has not been a contributor. In fact, it is been a net loser for the last 18 months as we've gone through this. We are positioning that business to be a mid-teens operating EBITDA business over there, as well as leaving us the capacity and the engineering skills to grow our engineering -- our energy business.

Justin Bergner

Okay. Got it. But that mid-teens would be on a meaningfully lower revenue base, I assume if you're taking that much cost out?

Joe Bartolacci

We are expecting that revenue base to be upwards of $80 million. No, this is -- by the way, Justin, that is just for OLBRICH, not the energy business as a whole.

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Justin Bergner

Got you. All right. And then if the Tesla situation is resolved, I mean, you wouldn't rule out new orders coming in as we look into fiscal year '25 from that customer as well, right?

Joe Bartolacci

I mean, look, we will take orders from anybody. We are taking orders, as I said earlier, from others. We are not at liberty right now to kind of speak more freely about that but we continue to take orders and interest levels are very high. As I said in my statement, this is a -- we've been saying it for a while. This is a solution that is tremendously valuable. It takes billions of dollars out of the process. What you are seeing is the reaction to that.

Justin Bergner

Got you. Totally understand, and all the best working your way through that lawsuit. Maybe lastly, in terms of noncore businesses, with your leverage and your refinancing, how are you thinking about some businesses that may be non-core within the portfolio within the next 12 to 24 months?

Joe Bartolacci

I mean, we're always looking at those. I would tell you that given where our debt position is and where we think that our Industrial Technologies business is going, we are now approaching that point where we think it's time to consider it more wholesomely, so we're considering everything right now.

Justin Bergner

Okay. And then lastly, just on the share repurchases, not a large quantity purchased in the quarter. Is it safe to say that those shares were purchased before you saw the Tesla situation coming to ahead? Or just any perspective on why you would deploy that capital in that way?

Joe Bartolacci

We did not buy a lot -- but it was also well before the situation with Tesla's -- the lawsuit. So that is not something that going into this environment we would be buying in today.

Operator

Thank you. Ladies and gentlemen, we have reached the end of question-and-answer session. I would now like to turn the floor over to Bill Wilson for closing comments.

Bill Wilson

Very good. Thank you, and thank you everyone, for joining us today and your interest in Matthews. We would encourage you for additional information about the company and our financial results. Please visit our website or contact me. Enjoy the rest of your day.

Operator

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

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