GMS, Inc. – Fiscal Third Quarter Earnings Conference Call Transcript
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David Matthew, *Baird*

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PRESENTATION

Operator:

Greetings, and welcome to the GMS Inc. Fiscal Third Quarter 2019 Earnings Conference Call. At this time, all participants are in a listen only mode. A question and answer session will follow the formal presentation. If anyone should require Operator assistance during the conference please press star, zero on your telephone keypad. As a reminder, this conference is being recorded.

I would now like to turn the conference over to your host, Leslie Kratcoski, Vice President, Investor Relations for GMS Inc. Thank you. You may begin.

Leslie Kratcoski:

Thanks. Good morning, and thanks to everyone for joining us this morning for GMS' Earnings Conference Call for the Third Quarter of Fiscal 2019 ended January 31, 2019. I'm joined today by Mike Callahan, President and CEO; and Lynn Ross, Chief Accounting Officer and Interim CFO.

In addition to the press release issued this morning, we posted presentation slides to accompany this call in the investors section of our website at gms.com.

On today's call, Management's prepared remarks and answers to your questions may contain forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. Forward-looking statements address matters that are subject to risks and uncertainties, many of which are beyond our control and may cause actual results to differ from those discussed today.

As a reminder, forward-looking statements represent Management's current estimates and expectations. The Company assumes no obligation to update any forward-looking statements in the future. Listeners are encouraged to review the more detailed discussions related to these forward-looking statements contained in the Company's filings with the SEC, including the Risk Factors section and the Company's 10-K and other periodic reports.

Today's presentation also includes the discussion of certain non-GAAP measures. The definitions and reconciliations of these non-GAAP measures are provided in the presentation and presentation slides.

Please note that references on this call to third quarter and fiscal 2019 relates to the quarter ended January 31, 2019, and the fiscal year ended April 30, 2019, respectively.

With that, I'd now like to turn the call over to Mike Callahan. Mike?

Michael Callahan:

Thanks, Leslie. Good morning and thank you for joining us today. I will begin today's call with a review of our operating highlights and some market commentary and then Lynn will cover our financial results in more detail. We will then open the line for your questions.

Now, turning to Slide 3, we were pleased to deliver a solid third quarter highlighted by record net sales and Adjusted EBITDA for both our reported and base business results. Our organic sales increase of 6.6% reflects strength and balance in both our product offering and the markets that we serve. We did face some challenges on the sales front, however, including lost shipping days associated with some abnormally wet, and extremely cold weather conditions in the quarter, and further softening in the Canadian single-family residential construction market.

Organic revenue growth was broad-based across each of our product lines with 3.9% growth in wallboard sales, 10.6% growth in ceilings, and 13.1% growth in steel framing.

Other product net sales were also up 4.5% organically. Now, on the profitability front, we generated a 41.5% year-over-year increase and Adjusted EBITDA to a record $59.7 million for the third fiscal quarter. The increase reflected contributions from Titan, increased operating leverage, including benefits from the cost-savings initiatives undertaken earlier this fiscal year, continued pricing improvement and favorable lease accounting.

Let me touch on a few of these areas next. In the third quarter, there was some further softening in the Canadian single-family residential market, which resulted in sales for our Canadian business declining low single digits on a constant-currency basis with further impact from about a 5% depreciation in the

Canadian dollar year-over-year. Nonetheless, Titan continues to be very accretive to our consolidated operating results. Our long-term strategic rationale for the acquisition of Titan, including increased scale and footprint in North America, geographic expansion into the highly attractive and fragmented Canadian market and creation of a well-balanced platform for growth remains very compelling.

The integration continues to progress well as we have continued to work closely with our key suppliers to generate purchasing synergies and take advantage of our scale and the power of our North American platform. With the commencement of our annual purchasing programs in January '19, we began to realize our purchasing synergies at the run rate associated with our previously announced $10 million target for purchasing synergies, and we continue to expect to exceed our original $10 million estimate for fiscal '20, and we continue to look for even more synergies with our cross-border suppliers and through other non-purchasing initiatives.

We have also continued to make progress on our previously announced strategic cost-reduction initiatives in the U.S. as demonstrated through the 130 basis points of operating leverage achieved during the fiscal third quarter, which excludes the impact of the change in lease accounting. As expected, we achieved full run rate savings as of January '19 and are on track to realize the full $20 million annual benefit of these initiatives in fiscal '20.

We generated strong free cash flow of $55.6 million during the quarter, which enabled us to reduce our net debt by $32.8 million and repurchase $11.5 million of our common stock under the repurchase authorization announced last quarter. We also opened a greenfield location just outside Akron, Ohio and this morning, announced the acquisition of Commercial Builders Group, LLC, subsequent to the end of the quarter. This tuck-in acquisition operates two facilities in the greater New Orleans and Baton Rouge, Louisiana markets, adding coverage of two important top 100 metro areas in the U.S.

As evidenced by all of these actions, we are executing on our stated and balanced capital-allocation strategies of debt reduction, disciplined growth through acquisitions and greenfields and opportunistic share repurchases.

I'd now like to spend a few moments explaining our current view of the end markets that we serve. Now, as a reminder, we estimate that approximately 55% of our consolidated revenues are to the commercial construction markets and approximately 45% is related to residential construction, with just less than half of that 45% related to new, single-family residential construction.

Since the latter part of calendar 2018, there's been a great deal of speculation with respect to the current macroeconomic outlook and the potential impact on residential and commercial construction. From our perspective, we remain encouraged by what we are seeing across our business and in the broader economy.

As it relates to residential construction, while it's still early in the traditional spring selling season, we believe the late '18 slowdown in new single-family residential construction was related to a confluence of factors, including a rise in interest rates, home-price appreciation and resulting affordability issues and geopolitical uncertainty. Like others, while we expect that this market may take a pause, we do not currently believe it will be prolonged or particularly deep.

Jobs and income growth remained at very healthy levels and many of the major markets in the U.S. continue to have limited housing supply, as building remains below historical average—averages, all of which bodes very well for the mid- to long-term outlook.

On the commercial front, which represents the majority of our business, most indicators and estimates point to continued growth against the backdrop of an economy that remains healthy. We are seeing that in our own business with strong backlogs and quote activity. In my recent visits to many of our locations in multiple geographies, I've heard from our own people and key commercial customers that pipelines are strong, extending through calendar 2019 and in some cases, even into calendar 2020. While it's impossible to predict what levels of growth are ultimately realized near term in the markets we serve, we remain focused on controlling what we can.

We believe our market-leading position in the distribution of interior building products, our balanced product portfolio and our diversified exposure across commercial and residential new and R&R construction markets, which we believe continue to exhibit healthy long-term fundamentals, will enable us to continue to take advantage of growth opportunities across our business, both now and in the future.

Looking to the balance of Fiscal 2019 and beyond, we remain committed to growing our business, both organically and through selective acquisitions, with an emphasis on profitability and free cash-flow generation, with which reducing debt remains a priority.

Now, with that, I will turn it over to Lynn for a more detailed review of the financial results. Lynn?

Lynn Ross:

Thanks, Mike, and would also like to thank you all for joining us on the call today. We were pleased to deliver a solid third quarter, highlighted by record net sales and Adjusted EBITDA performance and strong free cash flow generation.

Looking at Slide 4, we grew net sales 23.6% to $723.9 million, and increased our base business sales during the quarter by 6.6% compared to the third quarter of last fiscal year.

Our wallboard net sales increased 16% to $297 million in the third quarter compared to the same period last year, which was driven by acquisitions and pricing. The 3.9% growth on an organic basis was comprised of a strong pricing gain of approximately 4% and flat volume, the latter of which was due, in large part, to the lost shipping days in the U.S. and lower sales in Canada.

Our third quarter ceiling sales increased by 16.4% year-over-year to $105 million as a result of pricing improvement, higher organic volumes resulting from increased commercial business and the positive benefit of acquisitions. The 10.6% organic increase was comprised of price increases of approximately 7% as well as higher volumes of approximately 3%.

Our steel framing sales increased during the quarter by 21.4% year-over-year to $117.4 million. This was driven by strong pricing gains, acquisitions and higher organic volumes from greater commercial business. The 13.1% organic increase included price gains of approximately 10% and an uptick in volume of approximately 3%.

Our sales of other products, which consists of insulation, joint compound, tools, stucco and other complementary products totaled almost $204 million and were up 43.6%, compared to third quarter of last year. The recent acquisition of Titan has expanded the breadth of our product offerings, while at the same time, our 4.5% increase in our base business sales of other products reinforces the success of our efforts to continue to grow this other product category.

Our gross profit increased almost 20% to $234.2 million on higher sales, including the positive impact from acquisitions.

Our gross margin of 32.4% declined from 33.4% a year ago, primarily due to increased product costs as well as changes in product mix. Also, last quarter's third quarter gross margin was a tough comparison, being the highest gross margin level of any quarter last fiscal year and positively impacted by a higher level of supplier incentives associated with a larger level of wallboard pre-buy. Rising product costs over the past year included two wallboard increases, multiple steel and ceiling grid increases as well as various freight surcharges.

On a sequential basis, gross margin improved 20 basis points from the second quarter and slightly exceeded the 32.2% guidance we indicated in last quarter's call, which we continue to believe is a reasonable benchmark for the remainder of this fiscal year. Related to the announced wallboard increase, we believe we are well positioned to respond quickly to any changing price cost dynamics.

Turning to Slide 5. We reduced our adjusted SG&A as a percentage of net sales by 210 basis points year-over-year to 24.2% in the quarter, 130 basis points of the reduction was the result of increased cost efficiency, primarily due to the cost-reductions initiatives taken during this fiscal year as well as contributions from the Titan acquisition. These were partially offset by continuing inflationary pressures, primarily in logistics costs as well as higher costs from operating with the weather disruptions Mike referenced earlier. The remaining 80 basis points of the reduction was driven by changes to lease accounting.

As we've discussed, we've made significant progress on these reduction initiatives and we continue to find many opportunities to further streamline our business. As a result, we would expect fourth quarter adjusted SG&A as a percentage of sales to decrease year-over-year at least by the level we experienced in the third quarter.

We delivered $59.7 million in Adjusted EBITDA in the third quarter. This was up 41.5% year-over-year from $42.2 million in the prior year quarter. Adjusted EBITDA margin was 8.2% as a percentage of sales, or 7.4% if you exclude the impact of our lease accounting, which was up 20 basis points from 7.2% a year ago.

Turning to Slide 6. During the third fiscal quarter, we generated over $55 million of free cash flow. This enabled us to reduce our net debt by $33 million as well as repurchase $11.5 million of our common shares.

As of January 31, our net debt-to-LTM pro forma Adjusted EBITDA was 3.8x. This was consistent with the level as of the end of Q2. We intend to continue to de-lever through strong free cash flow generation. And as a reminder, our current leverage ratio, post Titan, compares favorably to 2014, when our ratio was 6x as well as just prior to our May 2016 IPO when it was 4.3x. Additionally, of our total long-term debt, approximately just over 75% is not due until 2025.

Also, in order to hedge against potential future interest-rate volatility, in February, we entered into an interest-rate-swap agreement. This agreement effectively provides a fixed rate on $0.5 billion of our first lien-term debt.

Our balance sheet remains healthy, with $74.3 million cash on hand, and $220 million available under our ABL facilities. This results in substantial liquidity for the business.

Now, let me turn the call back over to Mike before we open the line for questions.

Michael Callahan:

Thanks, Lynn. Just a few additional comments before we open the line for questions. We are pleased with our third quarter performance and believe that as a market-leading distributor of interior building products with significant scale advantages, combined with local expertise, we are poised for continued growth.

Our third quarter results provided further evidence of this, with sales and Adjusted EBITDA growth of over 23% and 41%, respectively.

We continue to take advantage of our multiple levers to drive this growth through organic growth, greenfields, M&A and operating leverage. We believe our large, diverse end markets continue to exhibit healthy fundamentals, providing us with significant growth opportunities across our business, both now and in the future.

And then finally, and probably most importantly, our great network of dedicated GMS employees in both the U.S. and Canada continue to embrace our strong entrepreneurial culture to deliver the outstanding service to our customers that we believe will deliver profitable growth over time to our shareholders.

With that, Operator, we're now ready to open the line up for questions.

Operator:

Thank you. If you would like to ask a question please press star, one on your telephone keypad. A confirmation tone will indicate your line is in the question queue. Please press star, two if you would like to remove your question from the queue. For participants using speaker equipment it may be necessary to pick up your handset before pressing the star keys. To accommodate as many questions as possible, we ask that you please keep to one question and one follow-up each.

Our first question comes from the line of Michael Wood with Nomura Instinet. Please proceed with your question.

Ryan:

Hey guys. This is Ryan calling on for Mike. Did logistics surprise you? Was this sudden? And could you just explain how logistics hurt SG&A? Whether this is freight rates or inefficiencies?

Michael Callahan:

Well, I think the short answer to that is, as I mentioned, there was definitely some impacts weather-related and the reality is, is that when you're dealing with production challenges, just in terms of getting loads out, your logistics and efficiency in terms of labor utilization is impacted. So, I would say that, that really was a key factor in how logistics impacted us in the quarter.

Ryan:

Okay, thank you, and then, just one follow-up. How did flat organic wallboard volumes compare to industry sell-through in your view?

Lynn Ross:

Yes, thanks for the question. In terms of how we compared to the industry, the Gypsum Association data, our read on that data is that we believe that we maintained share, we believe that most of the, both year-to-date decline and quarter-over-quarter decline at the Gypsum Association was due to the impact of pre-buys, so looking at that, we believe our flat volumes indicate that we're on par with our market share.

Ryan:

Thank you.
Operator:

Thank you. Our next question come from the line of David Manthey with Baird. Please proceed with your question.

David Manthey:

Thank you. Good morning.

Michael Callahan:

Hey, Dave.

David Manthey:

Good morning. First off, you mentioned that your gross margin percentage was lower due partly to higher product costs but clearly, your realized selling prices were higher also. I guess, this implies the price-cost relationship is negative, could you talk a little bit about that relationship? And, why did that happen?

Lynn Ross:

Yes, sure, thanks for the question. Related to the year-over-year decline in gross margins, this was due to, like we said, some changes in product cost and mix. In addition, the prior year comp was really impacted by a higher level of volume incentives that we realized in the third quarter of prior year due to the December 2017 pre-buy.

David Manthey:

Okay, thank you. Then, second, what is your outlook for price in the coming 12 to 18 months? I guess, we should assume a little bit less leverage on SG&A if your pricing moderates down. Is that your assumption?

Michael Callahan:

No, that's not our assumption at this point, I mean, as you know, day-to-day price—in terms of wallboard, the price increase is literally rolling out as we speak and then it took effect in the first part of March, so there have been announced increases. As always, it takes a period of time for it to settle out, but our assumption right now is to continue to look to the pending increase or the existing increase and see how it settles in. But we're not baking in a lower price environment for the year.

David Manthey:

I just meant more moderate price increases than last year, steel, for example?

Michael Callahan:

Oh, I'm sorry, yes. I would say, yes. I probably would say generally speaking, I think if you look at steel prices, they certainly have moderated, kind of flattened out, but I think that's a safe assumption, yes. The only caveat to that might be insulation. I think insulation is still on the bubble as it relates to the inflation.

David Manthey:

Great. Thanks, Mike.

Michael Callahan:

Thanks, Dave.

Operator:

Thank you. Our next question comes from the line of Trey Grooms with Stephens Inc. Please proceed with your question.

Trey Grooms:

Hey. Good morning.

Michael Callahan:

Good morning, Trey.

Trey Grooms:

Just real quick, I guess, kind of, following up with that—the last question is the—looking out on pricing, you mentioned maybe a little bit more moderate price increases. Were you talking specifically, just for clarity, around wallboard pricing? Or—and I know you mentioned steel, but wallboard pricing or ceilings, any—is it both? Or one or the other that you're referring to just for clarity?

Michael Callahan:

I would say that in terms of pricing going forward, wallboard, certainly, the increase, as I said is in the process of rolling out as we speak. I think in terms of ceilings, as we've often said, ceilings generally tends to price up, 2—1 to 2 increases a year, it's a 3% to 5% increase, generally speaking, on ceilings. Insulation, there still seems to be pressure on pricing as far as that goes, so I would anticipate maybe some inflation there, and—but steel has definitely settled down a bit and I don't see any near-term price increases there.

Trey Grooms:

All right, well, thanks for that. Just hearing that you were expecting more moderate, I just was making sure we were fully understanding that comment. Okay. Then secondly, is—the Canadian market has clearly weakened, was down this most recent quarter for you guys. What are you hearing from your customers there; their outlook for the building season in that market, as we're kind of at least starting to come into view with the building season here in Canada?

Michael Callahan:

Well, as the general backdrop, clearly, just this period of time tends to be a seasonal slowdown for Canada anyway, just based on the snow and cold conditions. I would say the outlook right now, on the single-family side there definitely has been some downward pressure, single-family detached, so the standalone homes definitely have seen—and a lot of that frankly has to do with the mortgage programs they have in place and the stress test that the Canadian government essentially has imposed on mortgages. So, that's definitely had an impact. But I would say that the—when you look at the commercial high-rise and commercial development as well as the commercial multifamily, and this pretty much goes across the board, the market outlook is still very positive. So, I would say, as far as Canada is concerned, it's pretty well—not completely isolated, but for the most part, it's that single-family detached business which is under pressure right now, but our view is still positive. I mean, I think the market overall is sound and the outlook is generally pretty optimistic.

Trey Grooms:

Okay. The last one from me is just on—with the increases that are out there, especially on wallboard, are you guys seeing or are you guys participating in any pre-buy of any size at this point?

Lynn Ross:

No, we've have limited pre-buy this season.

Trey Grooms:

All right, that’s it for me. I will pass it on. Thanks a lot.

Michael Callahan:

Thanks, Trey.

Operator:

Thank you. Our next question come from the line of Keith Hughes with SunTrust Robinson Humphrey. Please proceed with your question.

Keith Hughes:

Thank you. The EBITDA margins were up 20 basis points year-over-year, excluding the change in the leases. I assume—were your organic margins down given that Titan usually mixes you up? And if so, how much?

Lynn Ross:

Yes, thanks for the question, Keith. We don't break it down by those geographies.

Keith Hughes:

Okay. Let me ask you this way on Titan. You talked about sales being weak, if you, kind of—I know you didn't know that last year but just roughly, how did their margins look compared to last year, given the weak environment?

Lynn Ross:

Yes, Keith, they were lower and their SG&A, as a percentage of sales, was also impacted by the same weather conditions that we've discussed. And one thing on a constant-currency basis, sales were down 2%, the Canadian dollar did decline about 5% and that resulted in about a little bit less than $1 million of impact on their Adjusted EBITDA.

Keith Hughes:

Just one small question on this coming up fourth quarter, the interest expense we saw in the third, is that roughly—and tax rate; is that roughly what we'll see in the fourth quarter?

Lynn Ross:

Yes, that's a good way to think about the fourth quarter in terms of interest and taxes.

Keith Hughes:

Okay, great. Thank you.

Michael Callahan:

Thanks, Keith.

Operator:

Our next question come from the line of Matt Bouley with Barclays. Please proceed with your question.

Matthew Bouley:

Hi. Thank you for taking my questions. Mike, are you able to kind of quantify the impact of lost shipping days in the quarter? And then, maybe provide any comments around what you've seen, I guess, in February thus far? Thanks.

Michael Callahan:

Yes, thanks, Matt. It's really tough to quantify. The bulk of the impact in terms of weather tends to gravitate towards single-family and if you look at our numbers overall, our mix, you're probably looking 22%, 23% of our business overall is new resi, if you break it down on that basis. So, when you think about that, given just the magnitude of the impact the data had on the single-family piece, and it is—we lost numerous shipping days; it's not just the fact that it rains for 3 or 4 consecutive days, but it's also that you've to get the job sites themselves to dry out. So, while I can't relay quantify that, I think anybody that's been looking at the news and seeing it from Texas all the way to D.C., then we've all had to deal with pretty adverse conditions.

Now, we'll say that November, December were under a lot of pressure. January, we saw a significant pickup in momentum and activity, which carried over into February. So, I would say the momentum of activity in January, plus frankly, we were delivering on Saturdays trying to catch up, which also leads to some SG&A pressure, frankly, in terms of overtime and things such as that. So, if you bake all that together, so we're trying to catch up as best as we can, but fundamentally, I think, the January, February momentum levels give us cause for optimism going into the fourth quarter.

Lynn Ross:

Yes, I would note also that our February per day sales is up versus prior year on an organic basis.

Michael Callahan:

That's a good point.

Matthew Bouley:

Okay. I appreciate that detail. And then, secondly, just following up on the Titan business in Canada, and obviously you called out the challenges on the single-family side and that the data, seems to be a bit better on the multifamily side. Could you remind us of Titan's multifamily versus single-family exposure? And then just maybe put some finer points around what you're seeing on the multifamily side, specifically, because I do think the data has been a bit stronger there. Thank you.

Michael Callahan:

Thanks.

Lynn Ross:

Yes, they're—40% commercial construction and then 60% resi. On the resi side, about 40% new and then—and that's 40% of the total end market and 20% R&R, and we estimate on the commercial side that, that's 10% new and 30% R&R.

Matthew Bouley:

Okay. Appreciate the detail. Thank you.

Operator:

Thank you. Our next question comes from the line of Mike Dahl with RBC Capital Markets. Please proceed with your question.

Michael Dahl:

Good morning. Thanks for taking my questions.

Michael Callahan:

Good morning, Mike.

Michael Dahl:

Mike, I wanted to follow-up on the pricing comments again, I actually—2 parts of it, but first, on the wallboard side. I think Lynn mentioned, not really any pre-buy right now, and you're talking about seeing how the price increases settle out and they're early on, but is there anything to interpret in terms of how your viewing the market and the likelihood for price in terms of you guys not participating in pre-buy?

Michael Callahan:

Well, first off is the circumstances around pre-buy this year were different because the increase itself was pushed out, so routinely this is a January increase and it got pushed out this year. So—and then, of course, based on some of the conditions relative to deliveries, and some of the pressure, just the ability to find a place to put the board was limited, based on our inventory positions and delivery lags. So, the general outlook, Mike, is that we are going to be nimble as the price increase is introduced into the marketplace, but it's so—it's so early on, don't really know, a lot of it has to do with just demand levels and traction and takeaway for the plants, and that literally is taking place as we speak.

Now, the manufacturers continue to talk about escalating cost and inflationary pressures and they're reacting to that with their price increases, but the market will dictate just exactly how much of this ultimately is going to be realized, and depending on when it settles in, first, there may be a second phase to the increase, as they always leave the door open for that. So, I can't really handicap it at this point; we're going up as we received higher costs from our manufacturers. In many cases, we're requoting commercial work, requoting escalators, based on the projected increase and we have yet to see how it's all going to settle out.

Michael Dahl:

Okay. That's helpful. The second part of the pricing was really back—related to steel and comments about not expecting any further increases, I guess, given the path of steel pricing, when you look out over the next few quarters, do you think that we could see price declines actually?

Michael Callahan:

That's—that really is hard for me to call, based on the current—just the current uncertainties around steel in general and tariffs and everything else that's going on. What I will tell you, though, is that we have—our purchasing group here has a daily dialogue almost with the steel producers and we keep very, very close to the ground as to what's going on relative to steel pricing, and so our—we can move quickly too based on how we turn our inventories. I mean, our steel inventories cycle very quickly. So, even if there is a near-term price adjustment up or downward, we're able to cycle through that pretty quickly, based on our—just on how quickly we cycle the steel inventories. So, tough to handicap right now, I would say, right now, we look at it as, kind of, flattish and where it goes from here really remains to be seen based on demand levels and just consumption.

Michael Dahl:

Got it. If I could fit one more in. Lynn, you made a comment about the fourth quarter gross margin, I just wanted to understand or clarify that a little. Were you saying that the 32.4% seen in 3Q was still the reasonable assumption for 4Q? Or was that comment related to your prior 32.2%?

Lynn Ross:

Yes. No, our guide continues to be the 32.2%.

Michael Dahl:

Okay, great. Thank you.

Michael Callahan:

Thanks, Mike.

Operator:

Thank you. Our next question comes from the line of Kevin Hocevar with Northcoast Research. Please proceed with your question.

Kevin Hocevar:

Hey. Good morning everybody.

Michael Callahan:
Hey, Kevin.

Kevin Hocevar:

You mentioned that, so 3Q '18 had favorable gross margins for—you mentioned incentives ahead of price increases taking effect on the wallboard side and it sounds like you're not really pre-buying much ahead of this increase and gross margin expectations are—from 3Q to 4Q, relatively similar. So, can we infer from that, that you're not seeing the same level of incentives this year as you saw last year ahead of the price increases?

Lynn Ross:

The favorable—the favorability that we saw in our margin last Q3 due to the incentives was simply, I think, timing of the purchases. So, in terms of whole dollars or percentage, the incentives remain fairly constant; it's not even a little bit more favorable. So, no, I wouldn't infer that.

Michael Callahan:

Yes, I would agree.

Kevin Hocevar:

Okay. And then, so the largest wallboard manufacturer is set to be acquired here sometime in early 2019, so curious if you have any thoughts on that in terms of—do you expect that to have any impacts on that industry? Or do you think it will be pretty much business as usual after that transfer takes place?

Michael Callahan:

My view, having done business, significant business with both sides of that equation, so to speak, I think is going to be business as usual. I think it's going to be a very strong and formidable Company and they certainly have a very impressive array of products from the insulation side, all the way through wallboard and ceiling. So, from our vantage point, it's going to be business as usual and we're going to continue to do business with them as a combined entity, just as we have separately in the past.

Kevin Hocevar:

Got you. Okay. Thank you very much.

Michael Callahan:

Thanks.

Operator:

Thank you. Our next question come from the line of Matt McCall with Seaport Global Securities. Please proceed with your question.

Matthew McCall:

Thanks. Good morning everybody.

Michael Callahan:
Good morning.

Matthew McCall:
So, Mike, you mentioned comments—bullish comments about the mid to long term, specifically, on the residential markets. I was curious about more the near-term view. You said there may be a pause, I'm

just—I'm wondering about the impact of kind of the starts weakness that we saw in end of '18 and expected impact on your business to start '19, calendar '19?

Michael Callahan:

Well, I mean, I think it's logical to say that the same thing we were talking about in terms of weather impacts on our business has impacts on starts too. I mean, it's tough to clear land with a bulldozer when it's going to be submerged in six foot of water, like in a subdivision in Atlanta, Georgia. So, I mean, I think the reality is, our outlook is that if there is slippage, we think it's going to be moderate slippage because there's still a shortage of inventory, in just about every major market that we serve. So—and based on our conversations with the large national homebuilders that we do business with, if you add our footprint, that our house counts generally speaking are up, and I think the general attitude of the homebuilders is optimistic as well as the custom builders. It's just with the rate increases back at '18, carrying it over into a tough winter, I think the data is just, kind of, noisy right now. So, as we get deeper into the spring-selling season, I think all of us will have a bit better clarity on where this market is going to settle out. But, a pause, I think, is the best word because I don't consider it to be any kind of a long-term slippage. I think it's just a matter of making a temporary market adjustment, frankly.

Matthew McCall:

Okay. Thanks. That's helpful. The detail around the synergies and the cost saves that was also helpful. Can you—sounds like you're optimistic about meeting or exceeding those goals, but can you give us an idea of where you were as of Q3 for both the synergies and the cost saves and how we should layer those in over the next, I guess, 4, 5 quarters?

Lynn Ross:

Yes. Are you referring to the Titan synergies or SG&A synergies?

Matthew McCall:

Both, both. The cost saves and then the synergies as well.

Lynn Ross:

Yes, so on the SG&A—so, I would expect that for Q4 that our reduction in SG&A as a percentage of sales, our SG&A leverage, is somewhere between where it was Q2-over-Q2 and Q3-over-Q3.

Matthew McCall:

Okay. And then, is that, kind of—I think you talked about the total for—I think you said through 2020 for both synergies and cost saves, so I guess when do we hit the full run rate of each of those, both from Titan and the SG&A or the operational synergies?

Lynn Ross:

So, in terms of the full run rate on the Titan synergies, we just—those will both be 2020. Yes, those will both be 2020.

Michael Callahan:

Yes. We have the $10 million, the $10 million full run-rate synergies with Titan, which we expect to exceed, those we would be fully realized in Fiscal of '20, which is April of '20 and the same thing on the cost efficiencies or the cost savings of $20 million.

Matthew McCall:

Okay, all right. Thank you.

Operator:

Thank you. Ladies and gentlemen, this concludes our question-and-answer session. I'll turn the floor back to Mr. Callahan for any final comments.

Michael Callahan:

Well, thank you everybody for joining us today. We are very excited about where we are today, and we look forward to updating you on our progress in the coming quarters. Thanks for your time today.

Operator:

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