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Horizon Global Corp. (HZN)

Q4 2018 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning, everyone, and welcome to Horizon Global's Fourth Quarter 2018 Conference Call. My name is Christy and I will be your operator for today's call. All participants will be in listen-only mode until we reach the question-and-answer session of the conference call. This call is being recorded at the request of Horizon Global. If anyone has any objections, you may disconnect at any time.

I would now like to introduce Ms. Christi Cowdin, Director of Corporate Communications and Investor Relations for Horizon Global. Ms. Cowdin, you may proceed.

Christi Cowdin
Director-Corporate Communications & Investor Relations, Horizon Global Corp.

Thank you, Christy. Good morning, everyone, and welcome to our fourth quarter and full-year 2018 conference call and webcast. On the call today are Carl Bizon, our President and CEO of Horizon Global; Barry Steele, our Chief Financial Officer; and also Brian Whittman, our interim Vice President of Finance.

Earlier this morning, we announced our fourth quarter and full-year 2018 results. That release is available on many news sites as well as in the Investor Relations section of our website at horizonglobal.com.

Turning to slide 2, I would like to remind you that statements in today's presentation will include our views about Horizon Global's future performance, which constitute forward-looking statements. These statements are subject to risks and uncertainties that would cause or that could cause our actual results to differ materially from the forward-looking statements. We've described these risks and uncertainties in our risk factors and other disclosures in the company's most recent Annual Report on Form 10-K, Quarterly Reports on Form 10-Q and other filings with the Securities and Exchange Commission.

Today's presentation also includes some non-GAAP disclosures. These disclosures are reconciled to GAAP in the appendices to our quarterly press release and presentation, both of which are available in the Investor Relations section of our website at horizonglobal.com.

With all of that now being said, I would now like to turn the call over to our President and Chief Executive Officer, Carl Bizon. Carl?

Carl Bizon

President, Chief Executive Officer & Director, Horizon Global Corp.

Thank you, Christi, and good morning to all of you on the call today. This morning, we will be discussing our results for the fourth quarter and full year 2018. In addition, I'll be providing an update on our operations, our current business improvement plans and our outlook for the global business in 2019.

Both Barry Steele, who joined us as permanent CFO in February, and Brian Whittman, who served as interim CFO since November 9 of last year until Barry joined us, are with me on the call today. In a short while, Barry will take us through the operational performance of the business, and then Brian will provide an overview of our recent financing transaction. After that, we will open the call to questions from our covering analysts.

While I'm very glad to have Barry on board, I would like to take this opportunity to express my appreciation for Brian's dedication to Horizon Global and his efforts on behalf of the company.

As we discussed during our third quarter call back in November, we intended to seek an amendment to our existing credit agreement, which was achieved, but we were also successful in securing a second lien term loan to provide additional liquidity to ensure readiness for the upcoming prime selling season in the U.S. and allow for the execution of our business plans for 2019. These efforts are of key importance and support our longer term focus and goals.

As a company, we have been taking aggressive action now, and we'll continue to do so in order to position Horizon for long-term growth and profitability. There is still a lot of work ahead in 2019, but we have a fundamental belief in the underlying business and the dedication of our global team to execute the turnaround.

Today, we'll be discussing an overview of 2018 and the team's focus on the business improvement initiatives in Europe-Africa, as well as the collective efforts in the Americas to deliver a strong result for the prime selling season throughout the second and third quarters, actions that are expected to have a significant impact on improving the profitability of the company in 2019.

As a follow-on to the successful restructuring efforts in the Americas in 2018, we are further consolidating by moving our corporate headquarters to our Plymouth, Michigan location. We are also going to share more details regarding Friday's announcement regarding the new financing and related requirements for managing the business and paying down debt.

I believe it is prudent to continue my comments this morning by starting off with slide 4. Through the ups and downs and challenges of the last year, I'm proud that our team has remained focused on delivering best-in-class products to our customers and end users across all channels of distribution. We cannot, have not and will not lose sight of this.

Turning to slide 5, 2018 was a year of significant change. Challenges were identified in the business, plans were made to address these challenges, and the company went through a broad leadership transition to ensure we have a strong team, a team that is well equipped with the right mindset to execute the initiatives intended to return Horizon Global to improved performance and profitability.

2018 was focused on restructuring several aspects of our business and implementing operational improvement across our Americas and Europe-Africa business segments. In the Americas, we consolidated three office locations into one and restructured the regional team from the top-down to better align our internal resources and functions with the needs of our customers. These actions were substantially complete by the close of the third quarter. The Americas is now a more agile and responsive organization with a lower cost structure, which we expect to result in better service and improved profitability in 2019 and beyond.

The Americas team also spent a great deal of effort ramping up the region's new main distribution hub in Kansas City. Unfortunately, the process of establishing the facility and getting its performance to an appropriate level required significant effort throughout much of the year, including during the prime selling and shipping season in the second and third quarters of 2018.

Intense focus and effort from the team has resulted in the Kansas City facility now fully equipped with the capabilities, processes, and resources required to support our business and adjust throughput as needed to meet seasonal demand for 2019. As one important metric of this success, past due orders in the Americas decreased to approximately $6 million at the end of 2018 with about half being shippable orders, representing two days' sales. This is a further reduction from $8.5 million at the end of the third quarter and a seasonal peak of $26 million.

We replaced the Europe-Africa leadership team in late summer, utilizing our bench strength from the Asia-Pacific segment. The new team brings a fresh view and approach to the region and immediately went to work identifying performance and operational issues in the business. This new leadership team quickly identified key challenges facing the region and they accomplished a great deal in the final quarter of the year, including the scoping and phasing of near-, medium- and long-term business improvement initiatives intended to turn around this region. More on this in a moment.

We made top to bottom changes to our global management team. I was named interim CEO in May of last year, and then was named permanent CEO in October. Our new permanent CFO, Barry Steele, came on board in February.

Within our business operations, other significant management changes were made in both the Americas and Europe-Africa regions during 2018. I'm also pleased to announce that I am adding leadership responsibility for the Americas region to my current responsibility as CEO for the entire organization. This action will enable me to remain very close to the Americas and partner with the leadership team of our largest segment as we work to restore profitability in 2019.

In 2018, we successfully consolidated the Americas three offices into one and the resulting benefit is a leaner, more cost-efficient organization. We are pleased to announce further consolidation as a logical next step and we will be relocating our corporate headquarters to our Plymouth, Michigan location, which is also home of the head office of the Americas business.

We expect to realize some initial cost savings from this decision that will be related to reduced operating and facility expenses, but this action will have many benefits beside cost savings. We'll be able to support the team culture, increase collaboration opportunities and take advantage of synergies between many of the various functions in the business.

During 2018, we also experienced a great deal of impact from several external factors. Higher input costs, particularly steel, were not adequately offset by pricing or productivity initiatives in either our Americas or Europe-Africa regions. Additionally, increased global freight and logistics costs and a tight labor market in the U.S. negatively impacted our margin performance.

For 2019, we have instituted improved business processes to mitigate these impacts. And back in late 2018, we also introduced price increases in the Americas related to mitigate the announced tariffs.

Asia-Pacific continued to be a standout contributor to our company's 2018 results, and is expected to deliver another solid performance in 2019. Wherever possible, we leverage the skill sets and resources from this region across our global business to contribute to the company's collective efforts in product innovation, engineering expertise, and best-in-class manufacturing processes.

As I've shared earlier, in Europe-Africa, we are making progress on a series of business improvement initiatives intended to significantly improve operations and profitability in the region for 2019 and beyond. If we look at slide 6, I will touch on a few highlights of the business improvement initiatives that are being undertaken by the leadership team in Europe-Africa.

While progress was made in 2018 and many of the needed operational improvements and process fixes for Europe-Africa were identified, it will be a multi-year effort, as you can see by the timelines noted in the right column of the table on this slide. Several major initiatives are underway and half are targeted for completion within the 2019 calendar year.

Enhancing logistics to reduce freight costs and improve delivery times, while coordinating with our supply chain to increase overall efficiency is underway and expected to meaningfully reduce costs in the region. Efforts in our German, French, and Romanian production facilities are expected to maximize the efficiency of our operations, improve product quality, and reduce costs. But this will take time and attention to complete.

The theme that runs through nearly every element on this chart is that it's grounded in our efforts to simplify the operations and unwind unnecessary and unprofitable complexity across the region, while also focusing on recovering lost sales volume, which was caused by the challenges identified in 2018.

Our immediate objective is to stabilize Europe and mitigate any negative impact from the operations in the near term, so we can then establish a strong business platform to grow profitably in the region. We believe the issues in Europe are ultimately fixable with the right focus, effort and resources. Importantly, these initiatives are not associated with significant cash costs in 2019. The team continues to prioritize these initiatives, targeting those with the greatest potential impact on the most profitable programs, channels of business, production processes, and so on.

If we turn to slide 7, Barry will take us through the financials and segment results, and then Brian will walk us through the new financing and the amendment to our existing term loan agreement.

Barry Steele

Chief Financial Officer, Horizon Global Corp.

Thanks, Carl. Please turn to slide 7 for a review of the company's consolidated results for the 2018 fourth quarter. Our consolidated results are unfavorable to the prior year and weaker than anticipated. Net sales were 12.2%

lower during the fourth quarter of 2018 as compared to the prior year. A portion of this decline was due to unfavorable currency translation, but on a constant currency basis, the decline was still about 10%.

During the quarter, lower sales volumes and higher customer allowances were only partially offset by price increases implemented during the period. Further, the lower sales volumes were partly due to a difficult prior year comparison, which included special sales promotions that were not repeated in 2018, as well as sales from the Broom and Brush division that were divested in 2017.

Our 2018 fourth quarter operating loss of $29 million included $13.3 million in special items as compared to $6.9 million of special items during the prior year period. Fourth quarter 2018 special items are primarily comprised of distribution center inefficiencies and customer fines totaling $5.8 million, and adjustments to restructuring charges related to the reorganization activities in the Americas and Europe-Africa totaling $3.9 million.

Adjusting for these special items, the adjusted operating loss was $15.7 million for the 2018 fourth quarter, compared with adjusted operating income of $4.8 million for the fourth quarter of 2017. This decrease is mainly attributable to the lower sales volumes, unfavorable coverage of fixed costs, and higher freight and commodity costs, again only partially recovered by increased prices.

The unfavorable comparison between the fourth quarter of 2018 and the fourth quarter of 2017 is further driven by accruals made in the 2018 fourth quarter for settlements of legacy Westfalia claims and the reversal of our bonus reserve in a favorable IP settlement in the fourth quarter of 2017 in the Americas.

Now let's turn to slide 8 to review the segment performance for the quarter. The Americas and Europe-Africa segments both contributed to year-over-year decline in both net sales and adjusted operating profit. On the other hand, the Asia-Pacific region continues to deliver solid performance with nominal decreases in net sales and adjusted operating income due only to unfavorable currency translation. The decline in Americas' results were primarily driven by lower volumes, including the difficult comparison to 2017, which included the year-end sales promotion and higher customer allowances and retail penalties and higher input costs, primarily steel, labor and freight, which are only slightly offset by price increases.

The decline in Europe-Africa results were predominantly attributable to lower aftermarket sales in the United Kingdom, which drove an unfavorable margin mix for the region, higher raw material and freight costs attributable to the relocation of manufacturing operations from the UK to Romania, and accrued expenses related to customer claim settlements attributable to the legacy Westfalia business.

On slide 9, we show the full year consolidated results. 2018 was a year impacted by several operational issues, many of which have already been mitigated by various initiatives implemented during 2018 with full-year impacts of these initiatives as well as further actions expected during 2019. Net sales decreased by $43 million or about 5% as reported, and about 6% at a constant currency basis to $850 million, while operating profit of $35 million reported in 2017 swung to an operating loss of over $170 million for 2018.

Although the operating loss included many significant special items such as $127 million intangible asset impairment for the Europe-Africa segment. Our adjusted operating profit in 2018 decreased to $5.3 million from nearly $52 million in 2017. This significant reduction, combined with some of the special items requiring cash and growth in our working capital, drove our operating cash flow for 2018 to a negative $71 million, down from a positive $14 million during 2017.

Full year results from our operating segments appear on slide 10. In the Americas, net sales decreased by $49 million, or 11% to $391 million and adjusted operating profit declined by $28 million or 61% to $18 million. Operating challenges in this segment primarily centered around rising input costs and price availability issues in our new Kansas City distribution center. The cost increase included higher steel prices related to increased tariffs, higher freight costs related to a trucking shortage in the United States, and higher labor costs and labor retention issues at the Kansas City distribution center.

We began to offset these increases with corresponding price increases at the end of the year. But they came too late to have a meaningful impact on our 2018 results. The Kansas City distribution center was also impacted by price availability issues as a result of a slower than planned ramp-up of this new facility. The labor issues already I'd mentioned and delayed imports from China resulting from tight liquidity during the year. This in turn depressed our shipping volumes and caused significant retail customer penalties during our peak shipping season.

Our Europe-Africa segment also experienced significant declines in both net sales which decreased by less than 1% as reported, but by over 5% on constant currency to $323 million in an adjusted operating profit which decreased by nearly $19 million from adjusted operating profit of $5.7 million in 2017 to an adjusted operating loss of $12.9 million in 2018.

The challenges faced by this segment during 2018, included operational inefficiencies resulting from the consolidation of multiple manufacturing locations into our Brașov, Romania facility. This facility is dedicated to serving the aftermarket sales channel in Europe. Productivity at that Brașov facilities declined as it absorbs substantially more volume while at the same time material and transportation costs increased.

Decreased volume output resulted in lower aftermarket product availability and led to a reduction in net sales in our most profitable sales channel in the region. The Europe-Africa OE business also experienced unfavorable operating challenges attributable to increased deal and other commodity input costs which reduced our margins.

The Asia-Pacific segment reported stellar operating performance during 2018. Net sales grew by almost $9 million or nearly 7% to $136 million as reported and by over 8% in constant currency. Adjusted operating profit increased by almost 3% to $21 million due primarily to the higher sales volume.

Although we're not issuing formal 2019 guidance today, on slide 11, you will see a number of factors that we believe will drive significantly improved financial and operating performance in the coming year. First on the list are the activities that we have already completed which will provide benefits on a full year basis in 2018. These include a more stabilized distribution network in the Americas where we've already seen a reduction over time and improved operating efficiencies.

Our enhanced distribution network is expected to improve our sales volumes, customer fulfillment rates and reduced customer fines and penalties. Additionally, the work completed in 2018 to rationalize our operating footprint is expected to lower our operating overhead. And with this work completed, we will see a significantly reduced level of non-recurring charges in 2018.

Second, several initiatives that were begun in 2018 along with new actions already started in 2018 will begin to yield results in the coming year. For example, in the Americas, further price optimization and continued operational improvements in Kansas City such as the launch of an automated storage retrieval system are expected to improve our 2018 operating margins significantly.

As Carl mentioned earlier, the new leadership team in Europe-Africa is working to improve results for the segment. Examples include operating improvements from localization of our supply chain, surrounding the Romania manufacturing facility that are expected to lower input costs and improve aftermarket shipping performance. These improvements are expected to lead to higher aftermarket sales volumes.

Improvements in the European OE channel include a rationalization of the head count at our Rheda-Wiedenbrück facility in 2018, which focuses on our OE customers and higher sales volumes related to 2018 OE program launches.

Finally, when we developed our 2018 operating plan, we identified a number of measures, some of which have already been taken, that would provide additional flexibility as we navigate through the year and in particular through the very important summer selling season.

And now, Brian will provide an overview of our debt and liquidity position and the recent financing transactions.

Brian Whittman

Vice President-Finance, Horizon Global Corp.

Thank you, Barry. We announced in November that the company needed to amend its existing first lien term loan facility in order to modify financial covenants based on underperformance in the third quarter and expectations for performance in line with historical seasonality of the business until the 2019 summer selling season.

As Q4 unfolded, we solidified our plan for 2019. We determined that the company needed to raise additional liquidity to allow for a smooth summer 2019 selling season. Financing and amendment were completed this past Friday when the company closed on $51 million of new financing in the form of a second lien term loan and completed an amendment to our existing first lien term loan.

The amendment to our first lien term loan removes the prior leverage ratio covenant until the end of Q3 2019 and adjust the covenant at that point to a first lien leverage ratio aligned to our 2019 business plan. These actions represent an important step in preparing the company to maximize the 2019 summer selling season while positioning the company to reduce leverage over the long-term.

Together with the financing, the company is implementing changes at the board level with four new independent directors comprising a majority of the board to be seated in the near-term. We expect these new directors to bring fresh vantage points and industry specific skill sets. In addition, we will be undertaking a strategic review of our portfolio of assets to help determine our optimal structure going forward.

If we turn to slide 12, I'll review some of the specifics of our debt, working capital and liquidity position. During 2018, total debt increased $9.7 million in the fourth quarter driven by heavier borrowing on our ABL to fund underperformance in the Americas.

Working capital declined by approximately $26 million, generating additional cash flow as we collected receivable balances from the end of Q3 and moved into the low part of the year for sales. Our total cash and availability declined from $91.4 million at the end of Q3 to $53.4 million at the end of Q4, driven by operating losses as well as terminating a second facility in Australia which represented approximately $11 million of liquidity at the end of Q3.

Turning to slide 13. I'll cover a few additional highlights of our new $51 million second lien terms loan and the amendments to our existing $190 million first lien term loan. The term loan amendment eliminates prior financial covenants and puts in place a new set of covenants with the first lien leverage ratio test beginning with the reporting of our Q3 2019 results and set at 8.25 to 1. There was a 50-basis-point amendment fee and cash interest remained unchanged at LIBOR plus 6% with a new 3% paid-in-kind component.

The new second lien debt will earn LIBOR plus 11.5% paid in-kind through additional principal balance and had a 2% original issue discount, reducing the proceeds to the company to $50 million in the face amount of $51 million. At closing, the second lien lenders initially received warrants to purchase approximately 3.6 million shares of the company's common stock at $1.50 per share. In connection with the issuance of warrants to affiliates of greater than 5% shareholder of the company, certain lenders will receive preferred stock, which upon shareholder approval, will convert into additional warrants to purchase approximately 2.65 million additional shares of the company's common stock at $1.50 per share.

Overall, the new financing will provide approximately $40 million of incremental liquidity after accounting for fees and expenses of this facility, the first lien amendment, and the interim bridge financing that has now been repaid. The first lien amendment also called for the company to reduce the first lien term loan by $100 million over the course of the next 12 months through asset sales, a junior capital raise or a combination of both. A review of these alternatives will commence shortly. This review, combined with a focus on the continued turnaround of our operations, is intended to help reduce leverage and extend the maturity of the company's debt structure.

I'll now turn it back to Carl to wrap up our presentation.

Carl Bizon

President, Chief Executive Officer & Director, Horizon Global Corp.

Thanks, Brian. I have included slide 14 in our deck because I feel it crystallizes what we intend to achieve with our business. We intend to improve our operating performance by expanding margins improving profitability and ultimately generating cash to pay down debt and invest in the business.

For a company of our size, we need to tighten our focus, control the controllable, and simplify the overall business. With our enhanced leadership team and successful restructuring efforts, we're well positioned as a leaner, more agile organization that will be able to provide our customers with best-in-class service. Our shared resources, talents and focus on repeatable processes across our operations will strengthen the foundation of our organization and better position at company for future success.

Turning to slide 15. While many of the challenges from 2018 are clearly behind us, the team is intensely focused on the hard work required today, tomorrow, and beyond. We have reason for confidence in Horizon Global's underlying business. We have a leadership position in many major geographic markets and strong brands that resonate with our customers and end users around the world.

Continued strength in Asia-Pacific, a return to growth in the Americas and a continued progress on the turnaround in Europe-Africa provide the foundation for improved performance in 2019. The Americas entered the year with a leaner cost structure, a tested distribution network and improved business processes to mitigate commodity increases, tariffs and tight labor and freight markets.

As a stronger organization, we expect the Americans to realize financial benefits from the completion of its action plan, while it also delivers a greatly improved bottom line in 2019. While a great deal of work was done in 2018 to improve the structure and business approach in the Americas, the team continues to take a very prudent approach to manage costs in the business and mine for additional opportunities for efficiency or improvement.

The fine tuning of our Kansas City distribution center and the entire Americas distribution network has the Americas ready for its prime spring and summer selling season. However, it should be noted that as cold and wet weather conditions have persisted across most of the U.S., the season is off to a slow start. The unseasonable conditions are impacting numerous industries besides ours, but we are fortunate that many of our customers are still projecting a solid 2019 season albeit one with a late start.

I have shared a deeper view of the business improvement initiatives that are expected to turn around our Europe-Africa business, some, like increasing operational efficiency in our facilities in Germany, France and Romania are already underway and beginning to show results. Others such as regaining aftermarket market share in Europe and improving overall margin mix of our business will take time to realize. With the new financing agreement in place, we also have the liquidity and added capital needed to fund these business improvement initiatives and set the stage for long-term growth in revenues and earnings.

As Brian stated earlier, we have an obligation to pay down $100 million of debt in the next 12 months. Accordingly, we will undertake an in-depth review of our business to identify a range of options that will allow us to satisfy this obligation. We intend to achieve this requirement in a manner that serves our customers and employees and maximizes value to our shareholders.

Our team is aligned as one team with one goal. We have new talent throughout the organization and our global team is focused and determined to achieve our near and medium-term goals. Achieving our goals will establish a stronger base for the business, drive improved performance over the longer-term and deliver value for our shareholders.

I will now turn the call over to the operator, so we can take questions from our covering analysts. Operator?

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] And your first question comes from Matt Koranda of ROTH Capital.

Matt Koranda
Analyst, ROTH Capital Partners LLC

Q

Hey, guys. Good morning and welcome Barry. Looks like you just can't shake me.

Barry Steele
Chief Financial Officer, Horizon Global Corp.

A

Good morning, Matt.

Matt Koranda
Analyst, ROTH Capital Partners LLC

Q

So, just in terms of the 2019 outlook. I know we're not providing anything official in the release of the presentation this morning. But is there any reason that at least certain portions of the outlook that you shared back in February, and your lender presentation would not be valid today?

Barry Steele
Chief Financial Officer, Horizon Global Corp.

A

Nothing specific, Matt. We're obviously focused on delivering the best results possible. As Carl mentioned we do see a little softness in the start of this season. But I expect that we'll make it up at some point.

Matt Koranda
Analyst, ROTH Capital Partners LLC

Q

Okay. And then in particular, I guess, in terms of the weather softness guys, where specifically regionally is that impacting you guys for the season? And then how does that translate to how we should be thinking about Americas revenue in Q1?

Carl Bizon
President, Chief Executive Officer & Director, Horizon Global Corp.

A

So Matt, I think it's been very wet down south and it's been very cold up north. And we're talking to our customers who are telling us that they're being a little cautious in terms of filling their inventory in readiness for the season. I think we will see some slight delay related to a later spring than we would otherwise have expected.

But we have a number of initiatives that we have undertaken to offset some of that softness. And at this point in time, we still believe in the plan. We believe we have enough contingency measures that will offset what we're seeing and still believe in the numbers that we have projected for 2019.

Matt Koranda
Analyst, ROTH Capital Partners LLC

Q

Okay. And then you mentioned $6 million in past dues at the end of the quarter. Why didn't we push through all the past dues given Q4 is the lowest season I would have expected, you guys have the capacity to deliver on that. So any additional color there? And also just confirm, I think you said the $6 million is essentially half of that shippable in 2019?

Carl Bizon
President, Chief Executive Officer & Director, Horizon Global Corp.

A

Correct. So there is some inventory issues related to receiving materials from our suppliers, that has impacted the completion of some of our open orders. But the normal shippable past due is really within the operational range that we would experience in the normal course of business. So a day or two worth of past dues is, they could be one day overdue. It's just a normal part of the business. So when I think about past dues being sort of one or two days in total sales, that's about normal for an enterprise of this nature.

Matt Koranda
Analyst, ROTH Capital Partners LLC

Q

Okay. And then we still incurred some customer fines in Q4. So, just looking forward in 2019, I wanted to see if we could put a beta on sort of how much in customer fines that we should expect for 2019? And then maybe also just the cash restructuring number would be helpful?

Carl Bizon
President, Chief Executive Officer & Director, Horizon Global Corp.

A

So, when I think about the fines for 2019, we would expect them to return to sort of normalized levels. And traditionally, this business would see fines, which is again part of the retail aspect of our business. But that would be – expected to be less than $5 million. So, I think expectations for 2019 would be a number of certainly less than $5 million depending on obviously the performance of the business

Matt Koranda
Analyst, ROTH Capital Partners LLC

Q

Okay. That's helpful. And then, I guess, if we can cover the second main in the financing here for a moment. The requirement of a reduction in the first lien by $100 million over essentially, I guess the next 12 months, you guys mentioned a variety of options for sort of fulfilling that. Can you just elaborate a bit on sort of the timing of this path? I know you said you've engaged professional services to bring you down that pathway. But a little more color on the timing of that. And then how much of it is likely to be fulfilled by asset sales versus junior capital raise on the debt side versus equity?

Carl Bizon
President, Chief Executive Officer & Director, Horizon Global Corp.

A

So, Matt, I think it's fair to say that the process has started planning for this activity and an execution has commenced. In terms of whether it will be asset sales or the rising for the capital is something that will be assessed over time with the board. I think all options are available to us. And as we work through that process and the board assessed the options that are available to them, we will announce when appropriate which decision to be made.

Matt Koranda
Analyst, ROTH Capital Partners LLC

Q

Okay. I guess lastly just in terms of the covenants on the first lien that you guys adjusted, it looks like they kick in in Q3 2019 and you guys kind of get the full benefit or at least a partial benefit of the selling season. What is the actual ratio that you guys are held to in Q3 and going forward? I guess I can look at it in the literature here. But it'd be helpful just to get some color on that?

Carl Bizon
President, Chief Executive Officer & Director, Horizon Global Corp.

A

The covenants starts in Q3 with a first lien leverage ratio at 8.25, which is set at a significant cushion to our actual business plan to provide the company with significant flexibility as we work through the selling season in 2019.

Matt Koranda
Analyst, ROTH Capital Partners LLC

Q

Okay. Got it. You mentioned 20% I think cushion on that, right Brian?

Brian Whittman
Vice President-Finance, Horizon Global Corp.

A

It's actually higher than 20%.

Matt Koranda
Analyst, ROTH Capital Partners LLC

Q

Okay. All right. Got it. Helpful guys. I will jump back in queue here. Thank you.

Brian Whittman
Vice President-Finance, Horizon Global Corp.

A

Thanks, Matt.

Operator: Thank you. Our next question is from Josh Nichols of B. Riley FBR.

Josh Nichols
Analyst, B. Riley FBR, Inc.

Q

Yeah. Thanks for taking my question. I did want to ask, there's been a lot of movement recently in things like steel prices, also freight and labor. If you have any high-level commentary on what you've been seeing in that market over the last three to six months' trend and impact that could have on your business looking to 2019.

Carl Bizon
President, Chief Executive Officer & Director, Horizon Global Corp.

A

Hi, Josh. I think we are seeing a stabilization of steel prices from around the end of the fourth quarter. I think we saw a slight reduction as we headed into 2019. That seems to be holding, but it certainly is still substantially up over the levels we experienced in 2017. So despite the fact there has been some late small degree of softening, it is certainly substantial over the numbers during 2017.

In terms of freight, certainly, as the summer selling season impacted the volumes that were needed to ship in 2018, they were certainly elevated. Through seasonality, obviously, there is a greater availability of transport this time of year. So we're seeing some seasonal softening. However, I think it will be determined as we enter the peak volume season in Q2 and Q3 as to where the market ultimately prices road freight. As you know, it's a supply and demand commodity, so depending on need in the broader road transport industry, we'll see what happens.

Josh Nichols
Analyst, B. Riley FBR, Inc.

Q

And then – thanks for providing the slide with the update on the company's financial liquidity situation. Could you possibly provide a little bit more color on where the company stands as it is today as far as not just the debt level, but also the cash and the availability under the company's ABL?

Brian Whittman
Vice President-Finance, Horizon Global Corp.

A

The new financing with second lien debt improves our liquidity position after payment of fees by approximately $40 million. The cash levels are comparable based on seasonal, week to week, month to month fluctuations from where we have been recently.

Josh Nichols
Analyst, B. Riley FBR, Inc.

Q

Thanks. And then, could you talk a little bit about what you're seeing in the U.S. and Europe as it pertains to strength and/or weakness across the OE, the aftermarket and kind of the retail channels for those two segments?

Carl Bizon
President, Chief Executive Officer & Director, Horizon Global Corp.

A

The OE segment is still holding up well, Josh. I think there are some programs that we participate in that are performing better than others. And as you're aware, in the OE world, it is totally dependent on the particular manufacturer success with that particular vehicle in terms of how it affects our volumes. Some of those programs have been more successful than others, I would say. But in general, our volumes in the OE space are holding up.

In Europe, we have a number of new programs coming online, which will improve our OE volumes in 2019. And our Asia-Pac business continues to be very successful in obtaining new business across the broad spectrum of customers that they service.

In the aftermarket, around the world we are seeing – as we mentioned earlier, we're seeing a bit of a slow start to the aftermarket season, the peak selling season in the Americas. And, again, the European market has not yet come out of the sort of the winter seasonality.

In our Asia-Pac business, we're seeing good volumes and traditional strength from our very successful Asia-Pacific business through their summer selling season. As you know, it's the opposite to the Northern Hemisphere. So they are in the midst of their selling season now and they're seeing a continuation of good volumes as a result of their strong participation in the markets in Australia and New Zealand.

Josh Nichols
Analyst, B. Riley FBR, Inc.
Q

Thanks, Carl and Barry. That's all.

Carl Bizon
President, Chief Executive Officer & Director, Horizon Global Corp.
A

Thanks, Josh.

Operator: Thank you. Your next question is from Elizabeth Suzuki of Bank of America Merrill Lynch.

Elizabeth L. Suzuki
Analyst, Bank of America Merrill Lynch
Q

Hey, good morning. I'm just trying to quantify the impact that higher raw material costs and tariffs may have had in Horizon Americas and how much of that increase you were able to offset with price.

Barry Steele
Chief Financial Officer, Horizon Global Corp.
A

Are we talking about the fourth quarter or the full year?

Elizabeth L. Suzuki
Analyst, Bank of America Merrill Lynch
Q

In the fourth quarter particularly.

Brian Whittman
Vice President-Finance, Horizon Global Corp.
A

In the fourth quarter in the Americas, the higher input costs had about a $5 million bottom line impact during the quarter year-over-year.

Elizabeth L. Suzuki
Analyst, Bank of America Merrill Lynch
Q

Okay. That's net of price increases?

Barry Steele
Chief Financial Officer, Horizon Global Corp.
A

Sure.

Elizabeth L. Suzuki
Analyst, Bank of America Merrill Lynch
Q

Okay. I think you mentioned that some of your customers were holding off on building up inventory. I mean, do you think any of that is due to an expectation of tariffs potentially being reduced, which would mean those retailers might be able to push back more on price?

Brian Whittman
Vice President-Finance, Horizon Global Corp.
A

So, Liz, I think that is certainly playing into people's minds. I think whilst ever there is uncertainty around the U.S. government's position in relation to tariffs, I think that is certainly impacting some degree of caution around purchasing habits going in.

I think whether some of those parts ultimately receive the 25% tariff or hold 10% or even have those eliminated is still yet to be determined. But I'm sure that has some impact. But at some point in time, the market will need to respond to a demand from the consumer. And in any event that will happen, it's just to what extent and when. So whilst there could be some short-term hesitation, at the end of the day, when the market opens up through the summer selling season, demand will have to be filled, tariffs or no tariffs.

Elizabeth L. Suzuki
Analyst, Bank of America Merrill Lynch
Q

Great. And just finally, as you break out your buckets of costs and given that there's still lot of restructuring going on, what are your expectations for year-over-year increases in labor rates?

Barry Steele
Chief Financial Officer, Horizon Global Corp.
A

I think you see the normal inflationary levels, say, 3% in the U.S. and similar, maybe slightly less in Europe.

Elizabeth L. Suzuki
Analyst, Bank of America Merrill Lynch
Q

All right. Great. Thank you.

Carl Bizon
President, Chief Executive Officer & Director, Horizon Global Corp.
A

Thanks, Liz.

Operator: Thank you. That is all the time we have today for analysts' questions. I would now like to turn the call back over to Mr. Carl Bizon.

Carl Bizon
President, Chief Executive Officer & Director, Horizon Global Corp.

Thank you, everyone, for listening to the call today. I look forward to updating you further on our progress as we exit the first quarter and appreciate your support for the company. Thank you.

Operator: Thank you. This does conclude today's conference call. You may now disconnect.