08-Nov-2018

Horizon Global Corp. (HZN)

Q3 2018 Earnings Call

CORPORATE PARTICIPANTS

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

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

David G. Rice
Chief Financial Officer, Horizon Global Corp.

OTHER PARTICIPANTS

Josh Nichols
Analyst, B. Riley FBR, Inc.

Matt Koranda
Analyst, ROTH Capital Partners LLC

Elizabeth L. Suzuki
Analyst, Bank of America Merrill Lynch

MANAGEMENT DISCUSSION SECTION

Operator: Good morning, everyone, and welcome to Horizon Global's Third Quarter 2018 Conference Call. My name is Christi and I will be your operator for today's call. All participants will be in a 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, Christi. So, you've got two Christis coming at you this morning. So, good morning and welcome everyone to our third quarter 2018 conference call and webcast. On the call today are Carl Bizon, our President and CEO of Horizon Global, and also David Rice, our Chief Financial Officer.

Earlier this morning, we announced our third quarter 2018 results. The 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'd 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 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 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 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 third quarter and I'll be providing an update on our operations, the progress we've made against our Action Plan and our outlook for the global business. Dave Rice, our outgoing CFO, will update you on the financial results for the quarter in more detail. After that, we will open the call to questions from our covering analysts.

This will be Dave's last call as CFO of Horizon Global and I would like to personally thank him for his partnership during my time with the company. As we recently reported, we have a search for a permanent CFO underway and are confident we will identify an experienced financial executive with proven success in driving business improvements to join our team. Until a new CFO is named, we are fortunate to have Brian Whittman serving in the Interim CFO role. As we announced last week, Brian is a seasoned financial expert and I welcome his partnership in the interim.

Importantly, I want to express my appreciation for the confidence our board has placed in me by naming me permanent CEO of the company. This action is important for the continuity of our turnaround effort, but it does not change the longer-term focus and goals of what I've been working to accomplish here at Horizon Global.

As I have expressed many times since being named Interim CEO back in May, my position is to take aggressive action now to position Horizon for long-term growth and success. We have a significant job ahead of us, but in looking at the strength of our underlying business and markets, our brands, our customer relationships and most importantly our people, I believe in our ability to return to a path of profitable growth.

Each day, we are making progress as evidenced by significant steps taken in the turnaround of our business during the quarter. Namely, we completed the Action Plan in the Americas and are seeing results. Specifically, our Kansas City aftermarket and retail distribution center now has the capabilities, processes and resources required to support our business.

The facility can flex up or down to meet our seasonal needs. Our team remains hard at work identifying additional efficiency gains for our distribution network, including things like maximizing the use of our regional distribution facilities during peak times of the year, so we will be in a strong position for next year's prime season.

During the third quarter, we reduced our past due orders from a peak of approximately $26 million to $8.5 million, with shippable past due orders achieving normal levels at approximately two days' sales. During the third quarter, our new leadership in Europe-Africa conducted a deep assessment of the business. The team has begun making some significant changes in identifying business improvement initiatives for the near, medium and long term. More on this later.

Now, turning to slide 4, our team remains focused on delivering best-in-class products to our customers and end-users across all channels of distribution. This is vital. As a leadership team, it is our responsibility to ensure that our entire global team is aligned and equipped with the resources necessary to deliver each and every day.

On slide 5, we outlined some of the trends during the third quarter and Horizon's related performance. From a macro perspective, overall industry volumes in OE are beginning to moderate in Europe and the U.S., but we continue to perform well in this channel, with 21 new awards during the quarter, representing a full-year run rate of nearly $9 million in sales.

In early October, the team in Asia-Pacific delivered a key win for the company when Horizon won a repeat award of a long-term multi-year OE contract valued at $9 million annually. This result was achieved after a highly competitive process. We have not talked a lot about our Asia-Pacific business as our efforts have been focused on simplifying and improving our two larger business segments, but Asia-Pacific is a standout contributor to our company's performance.

The team consistently delivers strong financial results, but also makes many other important contributions to our business through efficient manufacturing processes, product innovation, engineering expertise and successfully integrating new businesses like the recent acquisition of Best Bars in New Zealand. We have and will continue to make a focused effort to leverage our Asia-Pacific team's talent and processes to positively impact the broader organization.

Back to the slide, the e-commerce trend continues to place pressure on both distributors and retailers in the global towing and trailering market. We expect this trend to continue, but also believe that brick-and-mortar retailers with strong in-store execution will continue to have a platform to compete with online retailers.

Horizon has strong relationships with both its e-commerce and brick-and-mortar retail customers and we have the resources and processes in place to meet their needs as the retail landscape continues to evolve.

Like many companies in our industry, we are not beyond the reach of U.S. economic policy and the related impact that includes steel cost inflation and tariffs on imported goods from China. Based on the recent implementation of the Section 301 tariffs and the additional tariff actions expected as of January 1, we are instituting price increases with our customers.

Additionally, just this week, we announced general price increases in the Americas due to rising labor, freight and commodity costs. We will continue to monitor our sourcing strategy in light of the evolving trade environment.

Dave will be taking you through a detailed review of our financial performance in just a few moments, but I want to highlight a few key items here. Please note that our third quarter reported results were again impacted by a non-cash impairment of goodwill in the Europe-Africa segment. However, the goodwill impairment does not affect our results on an adjusted basis or our cash flow.

A few notable points include consolidated revenue decreased 5% from a year ago. Our revenue for the quarter was most significantly impacted by the Europe-Africa segment, which experienced softness in both the OE and aftermarket channels. On an adjusted basis, we reported a loss of $0.01 per share for the third quarter. We have completed the Americas portion of our Action Plan, which I will speak to next.

And lastly, as I mentioned, new leadership in Europe-Africa has been assessing all aspects of the operations and has a fresh view of this business. They are working to determine the scope and phasing of near, medium and long-term business improvement initiatives expected to bring stability to this region and set a platform for future growth.

Turning to slide 6, this slide represents the Action Plan we have been working on during 2018. We have now completed all Action Plan items relative to the Americas segment. The facility closures, delayering of the organization and consolidation of the Americas team into one main headquarters are now complete.

The last major Action Plan item for the Americas was the improvement of the operations at our Kansas City distribution center. Kansas City is now operating at a level that can support the variable and seasonal needs of our business and we have significantly improved shipping volumes over the course of the quarter. Our team in Kansas City put forth tremendous effort to bring past due orders down to more normal levels.

At its peak, our unshipped past due orders were approximately $26 million and as at the end of the quarter, we brought that number down to $8.5 million with shippable past due orders representing approximately two days' sales. Of the remaining past due orders, the majority are the result of shipping delays from our suppliers in Asia, which we expect to improve in the fourth quarter.

The team in Kansas City has proven their ability to flex operations up and down in response to changing demand. And we have seasonally adjusted our [ph] shifts (10:56) and staffing to meet current demands. These adjustments are expected to improve our cost structures in Q4 and beyond.

With Kansas City now operating as it should, we are focusing on our core value proposition and rewarding the patience of our customers by providing the quality, innovative products and customer service they have come to expect from us.

As I indicated earlier, we have already begun planning in earnest for the 2019 busy season. Our aim is to ensure that we have the right products on our shelves and can meet the demands of our customers throughout the season from start to finish. We are fine-tuning the use of our Kansas City hub and our current broad network of regional distribution centers to meet demand.

With Kansas City having just reached its first birthday, we have worked hard to make progress in building strong relationships with freight carriers in the region. Perhaps most importantly, we have a strong leadership team in this facility that managed through one of our most difficult shipping seasons in recent memory. The learnings from these experiences are immense and further position us for a strong 2019 season. From here forward, we are focused on the normal day-to-day operational and process improvements that come with successfully managing a business.

While many of the recent Americas Action Plan initiatives greatly improved the cost structure of the business, the 2018 cost savings were invested to service our customers and optimize their selling seasons as we reduced past due orders. As we close out 2018, the Americas will enter 2019 with a leaner cost structure, a tested distribution network and a pricing strategy to mitigate commodity increases, tariffs and tight labor markets and freight markets.

With this stronger, leaner and better-managed organization, we expect to recognize financial benefits from the Americas Action Plan through a greatly improved bottom line in 2019. Due to the normal seasonality of our business, these results will not begin to meaningfully flow through our financials until we report second quarter 2019 results, but we are confident we will see performance ramp up in the interim.

You will note on slide 6, we have highlighted Action Plan items related to our Europe-Africa business as transitioning. As we communicated in August, we replaced this segment's management, operational and financial leadership. This new team has substantially completed its assessment of the business. The new team – the new leadership team has a very different view of the operations than the prior management team.

As you know, Jason Kieseker, who is deeply involved in the evolution of our Asia-Pacific operations and its strong performance over the last few years, has been charged with leading the turnaround effort in Europe-Africa. With this new leadership, we will have a capable and experienced team at the helm.

If we turn to slide 7, I will discuss our approach to Europe-Africa. First and foremost, the new team has determined that the operational status of Europe-Africa is sub-optimal. The synergies planned in connection with the integration of the Westfalia acquisition were intended to greatly improve the profitability of the Europe-Africa business. However, the execution and implementation of these synergy initiatives during 2017 and early 2018 ultimately did not deliver the desired result. In some instances, these initiatives added complexity and unintended cost in excess of the planned benefit.

We're taking a broader view towards Europe-Africa, transitioning from the Action Plan of 2018 to a new set of business improvement initiatives to the region. Our initial focus is to identify all challenges in the region and take the necessary steps to stabilize the business. While we are already making progress, the needed operational improvements and process fixes in the Europe-Africa business segment will be a multi-year effort.

The business improvement initiatives are still being defined and the phasing still being timed and we expect to be discussing Europe-Africa improvements for the foreseeable future. Overall, we will be focused on simplifying the operations and unwinding unnecessary and unprofitable complexity across the business.

The issues in Europe are fixable with the right focus, effort and resources. The team is currently determining the targets of that focus to the greatest impact on the most profitable customers, channels of business, production processes and so on. Our main 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.

Before turning the call over to Dave to review our financials, I want to reiterate our commitment to leading our team through this difficult transition period. Our company has a solid foundation and we have a fundamentally good business, despite the operational challenges we are facing today. We are a global leader in the towing and trailering industry, driven by our great brands, innovative products, solid engineering resources, reliable and efficient manufacturing operations, a strong customer base and a solid supply chain. As I've said before, we have all the ingredients for success here at Horizon Global, but we must execute.

Now, Dave will take you through the financials.

David G. Rice

Chief Financial Officer, Horizon Global Corp.

Thanks, Carl. In the commentary to follow, I will be discussing our performance in the quarter on an adjusted basis, excluding special items, which had been identified in the Appendix of today's presentation. Also included in the Appendix is a reconciliation of all adjusted non-GAAP results to the most comparable U.S. GAAP measure. References to earnings per share in my commentary refer to adjusted diluted earnings per share attributable to Horizon Global, excluding special items. Cash flow and balance sheet commentary will be on as reported U.S. GAAP basis.

With that, please turn to slide 8 for a summary of our third quarter results. As Carl presented, significant progress was made during the quarter on resolving the operational challenges in the Americas that negatively impacted the overall performance of the business during the first half of 2018. With the Americas Action Plan now complete and Kansas City shipping at more normal rates, the company's underperformance during the third quarter was primarily driven by our Europe-Africa business.

Third quarter sales of $227.8 million represent a 5.1% decline as compared to the same period last year, mainly attributable to a volume shortfall in Europe-Africa and the decline in the value of the euro and Australian dollar in relation to the U.S. dollar. Absent the impact of currency changes, net sales declined 3.6%. Net sales were slightly favorable year-over-year in our aftermarket, e-commerce and industrial channels. The remaining channels were down as the retail channel was constrained by inventory stock-outs on products from our overseas vendors, the delivery of which was delayed until the fourth quarter, and lower volumes on existing programs in the OE channel.

We finished the third quarter with operating income of $10.3 million, $7 million lower than the prior year. Majority of this decline was due to lower volume and unfavorable channel mix in Europe. Operating profit was also impacted by input cost headwinds, specifically metal and freight in advance of price realization, as well as incremental costs associated with production location shifts in Europe.

Based on the performance of the Europe-Africa segment in the quarter and the current outlook for that segment on a full-year basis, we recognized a non-cash goodwill impairment of $26.6 million in the third quarter, which eliminates the goodwill in this segment. This is a non-cash charge, which does not affect the company's ongoing operations or cash flows, but does reduce reported operating profit, net income and earnings per share on a GAAP basis. We have treated this impairment as a special item for purposes of evaluating the company's operating results and continuing activities.

Adjusted net income declined to a loss of $280,000 from income of $10 million in the prior year and loss per share for the quarter was $0.01 as compared to earnings of $0.38 in 2017.

Through the third quarter, we used $66 million of cash for operating activities compared to $2 million of cash used the same period in 2017. The elements of working capital reflected in increased use of cash during 2018 of $8 million as compared to 2017 primarily related to the timing of sales at the end of the third quarter of 2018 in an effort to bring trade payables back into terms.

Most significant elements of the increased use of cash are lower operating results, approximately $11 million in expenditures to execute our Action Plan through the third quarter and payments to terminate the Brink transaction at the end of the second quarter.

Total debt increased to $355 million compared to $321 million at the end of the second quarter and $279 million at the end of the third quarter of 2017. This increase is attributable to the $50 million in incremental term loan borrowings, partially offset by lower amounts outstanding on the ABL as compared to the second quarter.

LTM Bank EBITDA declined $22.8 million from Q3 2017, consistent with the change in operating profit, contributing to an increase in our third quarter leverage ratio to 6.7 times as compared to the 3.6 times at the end of the third quarter 2017. The Fourth Amendment to our Term Credit Agreement includes a leverage covenant of 7 times as of September 30.

Please turn to slide 9 for a summary of our segment performance. Third quarter net sales in our Americas segment of $116 million was flat with the same period last year. This reflects a significant reduction in past due orders that existed at the end of the second quarter and into the early part of Q3 as well as strong shipping activity at the end of the quarter. Revenue was up in every channel with the exception of retail, which was impacted by supply constraints from our overseas vendors.

Additionally, the favorable year-over-year revenue performance was achieved over the prior-year revenue that included sales from the Broom and Brush business, which was sold in the fourth quarter of 2017.

The Americas operating profit of $12 million or 10.5% of sales represents a 3.8% improvement over the same period last year and a margin increase of 40 basis points over the third quarter of 2017. While operations were still impacted by input cost headwinds only partially offset by pricing realizations, the benefits of the organizational restructure began to flow through the earnings in the third quarter. This result underpins the belief that the Americas' operational issues have been addressed and the business is ready to leverage the new structure as well as normal production and distribution environment in next year's prime season.

Performance of Europe-Africa is presented in the middle of the page. Net sales in the Europe-Africa segment declined approximately $9 million, with each sales channel lower than the same period in 2017. The aftermarket continues to be constrained by product availability, following the transfer of many of the channel's products to lower cost production facilities, while existing programs with major OEs have not achieved the volume levels they did in 2017. In addition, currency translation negatively impacted sales by $1.1 million as the euro weakened in relation to the U.S. dollar.

Operating profit for Europe-Africa decreased to a loss of $3.3 million, resulting from the revenue and channel mix headwinds described earlier in addition to input cost increases in excess of price realization. Additionally, the business incurred incremental charges as production moved to lower labor cost locations, but was burdened with additional freight and outside processing costs that in the aggregate more than offset any labor savings.

Performance of Asia-Pacific is highlighted on the right side of the page. The Asia-Pacific segment continues to perform in line with expectations. Net sales of $33.8 million declined by $2.9 million, of which, $2.1 million was related to the Australian dollar declining in value relative to the U.S. dollar. The balance of the decrease relates to lower volume on existing programs with OE customers, primarily impacting Thailand. For context, the business has been operating at historically high volume levels. So, this decline is not viewed as a reason for concern.

Q3 2018 also reflects the first comparative period for the business that includes the results of Best Bars, which was acquired in Q3 of 2017. Operating profit declined to $6.1 million or 18% of net sales compared to $6.9 million or 18.7% of net sales in the same quarter of 2017. Operating profit margin declined 70 basis points as a result of purchases from China and Thailand denominated in U.S. dollars and Thai baht respectively as well as a countrywide energy cost increase. These factors more than offset continued realization of benefits from previously-implemented productivity and restructuring initiatives.

Slide 10 is a view of our liquidity and leverage. We ended Q3 with a net leverage ratio of 6.7 times, relatively in line with our expectations and lower than our financial covenant of 7 times. This reflects an increase from 5.7 times at the end of the second quarter and 3.6 times at the end of the third quarter last year. LTM Consolidated Bank EBITDA declined $22.8 million from Q3 of 2017, as operating results from the current year replaced stronger quarters in 2017. Net debt increased to $355 million at the end of the quarter from $321 million at the end of Q2 and $279 million at the end of Q3 2017. This increase primarily resulted from additional borrowings relative to last year on the ABL to fund the operations of the company and the incremental $50 million borrowed [ph] on the (25:52) term loan.

We expect that our leverage covenant to be at its highest in Q3 and Q4 at the time we executed the Fourth Amendment to our term loan, but performance for the third quarter and the current forecast for the next 12 months reflect an underperformance as compared to expectations when we executed the Amendment. As a result, it is likely we will not be in compliance with the 7 times net leverage covenant for the fourth quarter of 2018 once reported. We are in active discussions with the administrative agent for the lenders regarding modification of the covenant terms and believe it is probable that an amendment will be obtained prior to triggering a default.

The revised view of near-term performance is disappointing and not a discussion we expected to have, but does not change our view of the underlying fundamentals of the business or expectations for the Americas and Asia-Pacific to deliver strong earnings in 2019. Europe-Africa is the primary driver of our revised view of near-term performance and as previously noted, we are evaluating and implementing business improvement initiatives in that region.

Cash and availability in our lending facilities of $91 million at the end of the quarter decreased approximately $26 million from $118 million at the end of Q3 2017, but has sequentially improved in the second quarter 2018 balance of $85 million. Cash generation of the business, combined with total availability under our revolving credit agreements, is expected to provide adequate flexibility for the demands of the business.

In closing, I'd like to leave you with a couple takeaways from our financial performance. The third quarter saw the stabilization of operations in the Americas as the Action Plan items in that segment were completed. We believe the business is positioned to succeed as it moves into the next selling season and the team looks forward to serving its customers at historical levels. As the new leadership in Europe-Africa commences improvement initiatives, we recognize that the recovery in that segment will take more time than the Americas, but the team is committed to consistent, steady progress toward the goals of the business.

Finally, it has been my privilege to be part of the Horizon Global team for the last 3.5 years. This is my last earnings call with the company, but I remain confident that Carl and the team, with support from Brian Whittman on an interim basis, will be successful as they continue to make operational improvements in the business. I firmly believe the focus on performance to the entire organization will be evident as the business moves through 2019 and beyond.

Now, if you'll turn to slide 11, I'll turn it back over to Carl to wrap up our prepared remarks.

Carl Bizon

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

Thanks, Dave. What Dave stated regarding our Q4 covenant expectation bears repeating. We are disappointed in our need to reopen discussions and seek additional amendment to our Term Loan Agreement, but we did not have the visibility into the Europe-Africa business as we do now. With new leadership in place in the segment, we have established a fresh view of the business and are developing and executing a related set of business improvement initiatives intended to deliver expectations for our company's European-based business.

Turning to slide 11, it has been a little less than six months since the board brought me in to lead our turnaround and in that short amount of time, we have made solid progress. We identified key areas to address in our Action Plan, completed the Americas' actions and replaced several top leadership roles across our global team. We are nearing completion of our assessment of Europe-Africa and targeting areas for improvement.

As a result, we are moving with speed to define a process and timeline for prioritizing and implementing business improvement initiatives in the region. We have reason for confidence in Horizon Global's underlying business. We have a leadership position in many major geographic markets, significant manufacturing and distribution resources, engineering and product development expertise, solid suppliers and a loyal patient customer base, all of which will help steer us through this transition.

We completed the Americas Action Plan and have broadened our scope of considered business improvement initiatives in Europe-Africa. We have adopted a more operationally-focused approach to our business in Europe that will take time to achieve, but we see a clear path to improvement.

Driving productivity and profitability improvements across our businesses are the cornerstone of my approach to running this business and are at the forefront of every decision we make as a company.

Despite the many great changes in our organizational leadership and structure, 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 succeed by establishing a stronger base for the business to drive improved performance over the longer term. We are laser-focused on improving the profitability of our company, generating cash to pay down debt and restoring the confidence of our employees, our customers and 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. The floor is now open for questions. [Operator Instructions] And your first question comes from Josh Nichols of B. Riley FBR.

Josh Nichols
Analyst, B. Riley FBR, Inc.

Q

Yeah. Hi. Thanks for taking my question and congrats, Carl, on the appointment to permanent CEO. I want to ask, you did mention in the deck and on the commentary that you're seeing growth in OE business begin to moderate a bit in the European and U.S. markets. Could you talk a little bit about what you think the driving forces are behind that?

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

A

[ph] I guess (31:55) there's some general change in economic circumstance in some of the markets. And whilst we're seeing some volume change in some of our programs, the mix overall around the globe is positive to the programs we have. We're seeing reductions in Sedan-based volume, but seeing ongoing growth in SUVs and pickup trucks both in Europe and in the Americas.

So, I think, overall, whilst we're seeing some moderating, the outlook is still good. Our mix is still favorable and I still feel positive about our participation in the right areas in the OE market.

Josh Nichols
Analyst, B. Riley FBR, Inc.

Q

Thanks. That's helpful. And then, could you talk a little bit – with a little bit of a – bit more information or a breakout of some of the items impacting the gross margin line as far as steel, freight and tariffs?

David G. Rice
Chief Financial Officer, Horizon Global Corp.

A

Yeah. So, in terms of the impact on gross margin, there's one you missed there. We've been talking about input cost increases for quite a while. Up until recently and recently being sort of the beginning of Q3, we had not seen tariff impact, but we began to see that through Q3 and reacted with pricing as Carl mentioned.

The piece that's really been identified through the team in Europe is all of the incremental costs that we've incurred on products that we've moved to lower-cost manufacturing locations throughout the region, so specifically transfers from the UK and Germany to either Romania or South Africa. While we're definitely getting the labor arbitrage associated with the assembly of those products, the incremental freight we've incurred, either to move product or component to down South Africa and then completed product back-up or around Europe, including outside painting and other outside processes, have more than offset those savings.

So, really that's where we're seeing the bulk of the increase. We've addressed it clearly with the pricing discussion that Carl gave in the Americas on all of those fronts, input costs as well as tariffs, and really are looking to do both in Europe, so both pricing as well as undoing some of those moves that added to those incremental gross costs.

Josh Nichols
Analyst, B. Riley FBR, Inc.

Q

And then, last question for me, then I'll hop back in the queue. Have you seen any customer losses, given some of the issues, particularly in Europe, with the companies working through at this point? And at a higher level, a hard question to answer I'm guessing at this point, but how long do you think it may take before we see operating performance in Europe-Africa begin to improve on a year-over-year basis?

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

A

I think to answer the first part of your question, the aftermarket business is essentially a stock availability position. And I think whilst in Europe the inventory levels and service levels have been somewhat impaired by the focus on moving production around Europe, we have longstanding relationships with our customers in Europe and I'm looking forward to Jason's focus on not only improving our inventory position, but ensuring that we have the right product set as we approach the northern hemisphere selling season next year. So, I think whilst there would have been some volume loss from existing customer base, that would be the key to any revenue shortfall in Europe.

The same goes in the Americas that effectively the aftermarket business is a stock availability business and our ability to service that market at a Kansas City has impacted overall volumes in the quarter. But as we mentioned earlier, we have made substantial progress in the Americas to resolve the issues around Kansas City and we look forward to participating in those markets in a much leaner, stronger, more focused way in the coming year.

Josh Nichols
Analyst, B. Riley FBR, Inc.

Q

Thanks, guys.

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

A

Thanks.

Operator: Thank you. Next question is from Matt Koranda of ROTH Capital.

Matt Koranda
Analyst, ROTH Capital Partners LLC

Q

Hey, guys. Good morning. Congrats, Carl, and best of luck, Dave.

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

A

Thanks, Matt.

Matt Koranda
Analyst, ROTH Capital Partners LLC

Q

So, on Europe, just in terms of the higher-level improvement bullets, that's appreciated, but I guess I was expecting maybe more quantifiable metrics in terms of timing and the magnitude of improvement they anticipate over the next 12 months or so. Just any sense for when you'll be able to share more quantifiable metrics as it pertains to sort of like either long-term normalized operating margin expectations or sort of the magnitude of improvements that you might expect with the initiatives that you're enacting on a year-over-year basis?

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

A

I think the position with Europe is something that is under – the position is evolving in terms of the Action Plan. We know what we have now. The new team has been on the ground for a couple of months. And I think when we look forward into the programs and the initiatives we're going to take in the coming period, it's a multitude of different actions in different areas. And as we identify and quantify some of those going forward, we will provide greater detail, probably at the end of the year or through the coming year, but it is going to be a long process. There is much to be done.

The easy quick wins are being taken now, but some of the more structural longer-term decisions will take time to flesh out as we learn more about the circumstances we find ourselves in Europe. So, I think you'll see constant progress over time, but it will take a number of years before we get to a position that we're ultimately happy within Europe. We expect improvement in the coming year and we expect improvement to continue over the years beyond that.

Matt Koranda
Analyst, ROTH Capital Partners LLC

Q

Okay. Just in terms – maybe just digging into some of the things in the bullet points you just provided, just to try to flesh out a bit more, so optimizing your operational structure in the second bullet on that slide that you provided, does that mean shutting additional facilities? Are you comfortable with your low-cost country footprints or will other changes need to be made in terms of the improvement plan there as well?

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

A

That's part of the assessment. Jason and I have had many discussions around our operational footprint in Europe and I think as we start to stabilize our view of what's made where and the cost of what is made where and the supply chain complexities that follow the decision – those decisions will be in a position to provide greater detail.

But as it stands right now, we are still evaluating, evolving those decisions. So, I think over the coming months and the coming year, broader decisions we made about what we make where and how we do it.

Matt Koranda
Analyst, ROTH Capital Partners LLC

Q

Okay. And then, the one other item I wanted to cover on that slide was just in terms of the customer base and channel focus that you guys referenced. I mean does that mean that we're going to walk away from certain customers that – or maybe in channels that are less attractive? Maybe could you just comment on the relative attractiveness preliminarily of at least maybe the aftermarket versus OE in Europe and how you view those?

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

A

I think when we acquired the Westfalia business, we acquired a book of business that some of which was contracted. [ph] We were in programs that were entrained (39:56) when we acquired the business. Some of those programs have particular margin profiles that – some of them we may choose to participate beyond that current program, others we may choose to not rebid and seek alternative more attractive business. I think that's the good thing about our business around the globe is we have the ability to select or de-select business in the interest of the organization.

The aftermarket is the secondary channel in Europe. Certainly, OE – whether it's OEM or OES is our primary channel, but I think as we evolve that business and the footprint of that business in the coming years and programs were all off and new programs were all on, we will be making constant improvements to the customer and margin mix of the revenue we have in Europe.

So, I think it's a combination of the revenue and margin we acquired and the revenue and the margin that we acquired going forward from here based on our view of what makes sense based on where we are, how we make it and the margins that accrue from that business. So, it's an ongoing process that we're quite familiar with and something that we do on an ongoing basis either in Asia-Pacific or in the Americas.

Matt Koranda
Analyst, ROTH Capital Partners LLC

Q

Okay. And then, any stab at maybe what the incremental cash restructuring needs will be in Europe-Africa, as you kind of move through with this plan? Will you need additional cash to get this done? Are you comfortable with where the balance sheet sits currently to kind of – are you capitalized enough to sort of get this stuff done with the existing cap structure?

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

A

I think that's to be determined. And at the moment, we're operating within our facilities.

Matt Koranda
Analyst, ROTH Capital Partners LLC

Q

Okay. I guess why go through this as a public company, I mean why not just initiate sort of strategic alternatives? It just sounds like Europe is going to take couple of years at least to get sorted. It's going to be potentially challenging over the next couple quarters as you guys alluded to. Any thoughts there?

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

A

I think the board assess options on an ongoing basis and I certainly can't speak for the board in that regard. At the moment, we are focused on executing the plans we have for the company and the board will make those assessments as time goes on. Right now, we're focused very clearly on fixing the company and getting ourselves in a position of operating performance that is satisfactory. And that's my focus right now.

Matt Koranda
Analyst, ROTH Capital Partners LLC

Q

Okay. I'll leave it there, guys. Thanks.

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

A

Thanks, Matt.

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

Elizabeth L. Suzuki
Analyst, Bank of America Merrill Lynch

Q

Great. Just on Asia-Pacific, you had noted that you had your first quarter of sales declines even backing out the currency impact and then you mentioned a small decline in existing programs. It seems like this has been a pretty steady growth region for a while on a constant currency basis. So, what do you attribute that decline in existing programs to? Like what changed in the third quarter?

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

A

Liz, to be honest with you, the magnitude of the change was very, very small. The business operates very strongly in a region that is somewhat constrained in terms of size and available market. We're very pleased with the operations of that business. I think in the scheme of things, the business has done very well. Certainly, I think the magnitude of the change is something like $800,000.

David G. Rice
Chief Financial Officer, Horizon Global Corp.

A

Yeah.

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

A

And it's not substantial in the overall scheme. I think the business continues to operate very well, has strong relationships in its region and has a very good market position.

David G. Rice
Chief Financial Officer, Horizon Global Corp.

A

And that's why I made the comment I made, Liz. There's nothing underlying the change that suggests that programs are dying or we're not getting replacement business or anything like that at all. It's simply just [ph] there are no competitors (43:55) in this particular 90-day period compared to last year at the same time.

Elizabeth L. Suzuki
Analyst, Bank of America Merrill Lynch

Q

Got it. Okay. So, there aren't any like macro headwinds that you would point to or anything like that that you think is changing more broadly in Asia-Pacific?

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

A

Not at all, Liz.

Elizabeth L. Suzuki
Analyst, Bank of America Merrill Lynch

Q

Okay. And then, second, can you just remind us how your covenant requirements progress over time? I think I recall that the leverage ratio needs to step down pretty aggressively over the next several quarters. I mean do you plan to amend those medium-term levels in addition to that near-term 7 times maximum?

David G. Rice
Chief Financial Officer, Horizon Global Corp.

A

That's part of what we're in conversations with our administrative agent on. So, we're putting together our best view of the business and part of those discussions will be precisely what relief we're looking for as Europe plays out.

Elizabeth L. Suzuki
Analyst, Bank of America Merrill Lynch

Q

Okay.

David G. Rice
Chief Financial Officer, Horizon Global Corp.

A

So, more to come.

Elizabeth L. Suzuki
Analyst, Bank of America Merrill Lynch

Q

Great. Thank you.

Operator: Thank you. At this time, we have no further analyst questions. I would like to turn the call back over to Mr. Carl Bizon for any additional or closing remarks.

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

I'd like to thank you all for joining the call today. And I look forward to updating you in the future as our plans progress. Thank you.

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