PrecisionIR Group

PrecisionIR Group
9011 Arboretum Pkwy
Suite 295
North Chesterfield, VA
23236

Phone: 804-3273400
Fax: 804-327-7554

www.precisionir.com
www.investorcalendar.com
www.companyspotlight.com

Transcript of
Astec Industries, Inc.
Second Quarter 2013 Earnings Call
July 23, 2013

Participants

Stephen Anderson – VP of Administration, Director of IR and Secretary
David Silvious – Chief Financial Officer, Vice President and Treasurer
Don Brock – Chairman, Chief Executive Officer
Ben Brock – Vice President, Asphalt

Analysts

Jack Kasprzak – BB&T Capital Markets
Richard Wesolowski – Sidoti & Company, LLC
Brian Brophy – Robert W. Baird
L. Todd Vencil – Sterne Agee & Leach
Jason Ursaner – CJS Securities, Inc.
Ted Grace – Susquehanna Financial Group
Morris Ajzenman – Griffin Securities
Brian Rafn – Morgan Dempsey

Presentation

Operator
Greetings, and welcome to the Astec Industries Second Quarter 2013 Earnings Call. At this time, all participants are in a listen-only mode. A brief question and answer session will follow the formal presentation. As a reminder, this conference is being recorded.

It is now my pleasure to introduce your host, Steve Anderson, Vice President of Administration.

Stephen Anderson – VP of Administration, Director of IR and Secretary
Thank you, Jesse. Good morning, and welcome to the Astec Industries conference call for the second quarter ended June 30, 2013. As Jesse mentioned, my name is Steve Anderson and I'm the Vice President of Administration, Secretary, Director of Investor Relations for the company. Also on today's call are Dr J. Don Brock, our Chairman and Chief Executive Officer; Ben Brock, Vice President of our Asphalt Division; and David Silvious, Chief Financial Officer. In just a moment, I'll turn the call over to David to summarize our financial results, and then to Don to review our business activity during the quarter.

Before we begin, I will remind you that our discussion this morning may contain forward-looking statements that relate to the future performance of the company, and these statements are intended to qualify for the Safe Harbor liability established by the

PrecisionIR Group
9011 Arboretum Pkwy
Suite 295
North Chesterfield, VA
23236

Phone: 804-3273400
Fax: 804-327-7554

www.precisionir.com
www.investorcalendar.com
www.companyspotlight.com

Private Securities Litigation Reform Act. Any such statements are not guarantees of future performance and are subject to certain risks, uncertainties and assumptions. Factors that can influence our results are highlighted in today's financial news release and others are contained in our annual report and our filings with the SEC.

At this point, I'll turn the call over to David to summarize our financial results for the second quarter of 2013.

David Silvious – Chief Financial Officer, Vice President and Treasurer
Thanks, Steve. We appreciate each of you who are listening in for your interest this morning. Net sales for the quarter were $248.1 million in 2013 versus $238.3 million in the second quarter of '12. That's about a 4% increase, about $9.8 million.

International sales for the quarter were $85.8 million, compared to $83.9 million in the second quarter of '12. That's a 2% increase, about $1.9 million. International sales were 34.6% of second quarter 2013 sales, compared to 35.2% of second quarter of 2012 sales. The increase in the international sales for the second quarter of '13, compared to the second quarter of '12, occurred primarily in Africa, in the West Indies and the Middle East and in Brazil. These increases were offset by a decrease in Canada.

Domestic sales for the second quarter of '13 were $162.3 million compared to $154.4 million in the second quarter of '12. That's a 5% increase or $7.9 million. Domestic sales were 65.4% of the second quarter of 2013, net sales compared to 64.8% for the second quarter of 2012 sales. Parts sales for the second quarter of '13 were $62.7 million compared to $60.1 million for the second quarter of 2012. That's a 4% increase or $2.6 million. Parts sales were 25.3% of the quarterly sales in 2013 compared to 25.2% in the second quarter of 2012.

Aggregate and the Mining Group had the largest dollar increase in part sales, followed by the Asphalt Group and the other group, compared to the second quarter of 2012. The Mobile Asphalt Paving Group and the Underground Group each had small decreases. On a year-to-date basis, net sales were $496 million, compared to $490.2 million in 2012, that's a 1% increase or $5.8 million. International sales on a year-to-date basis in '13 are $171.7 million compared to $180.8 million in '12. That's a decrease of about 5% or $9.1 million. The decrease in international sales occurred primarily in Australia, the post-Soviet States and in South America. These decreases were offset by increases in Europe, Africa and the West Indies.

International sales were 34.6% of net sales for 2013, compared to 36.9% for 2012, all on a year-to-date basis. Domestic sales on a year-to-date basis in '13 were $324.3 million compared to $309.4 million in 2012. That's a $14.9 million increase or 5% increase. Domestic sales are 65.4% of 2013 total sales year-to-date, compared to 63.1% of total sales in 2012 year-to-date.

Part sales year-to-date are $130.8 million compared to $132.9 million in 2012. That's about a 2% decrease or $2.1 million. Part sales were 26.4% of total sales for 2013 year-to-date compared to 27.1% of total sales year-to-date 2012.

Gross profit for the quarter was $55.4 million in '13, compared to $53.1 million for the second quarter of 2012. That's a $2.3 million increase or a 4% increase in gross profit dollars for the quarter. The gross profit percentage was flat at 22.3% for both Q2 of '13 and '12. One major impact that we had during the quarter was a negative impact from the absorption variance of about $7 million, and that occurred primarily in the Asphalt Group and in the Aggregate and Mining Group.

PrecisionIR Group
9011 Arboretum Pkwy
Suite 295
North Chesterfield, VA
23236

Phone: 804-3273400
Fax: 804-327-7554

www.precisionir.com
www.investorcalendar.com
www.companyspotlight.com

On a year-to-date basis, gross profit was $114 million compared to $111.7 million for the year-to-date 2012. That's a 2% increase or about $2.3 million. Gross profit percentage as a percentage of sales on a year-to-date basis is 23% compared to 22.8% on a year-to-date basis in 2012.

SGA&E for the quarter is $37.8 million or 15.2% of sales compared to $38.5 million or 16.1% of sales for the second quarter of 2012, a decrease of about $700,000 in dollar terms and a decrease of about 90 basis points as a percentage of sales. The big decrease that we had there is primarily in the Research and Development expenses. For the year, SGA&E was $78.2 million or 15.8% of sales compared to $78.6 million or 16% of sales or a $400,000 decrease. Again, the big decrease there on a year-to-date basis, contributing there was Research and Development expenses.

Income from operations increased to $17.6 million in the second quarter of '13 from $14.6 million in the second quarter of '12. That's a $3 million increase or a 20% increase. On a year-to-date basis, income from operations is at $35.8 million compared to $33.1 million for the year-to-date 2012. It's a $2.7 million increase or 8%. Sales and income by segment are attached to your press release for your reference.

Now for the tax rate, the effective tax rate on continuing operations for the quarter is 36.6% compared to 36.9%, so only down slightly on continuing ops for the quarter. For the year, we're at 33.1% compared to 37.3% for the year-to-date period in 2012 and if you recall, that's primarily driven by the Research and Development tax credit, which was not in effect in 2012, but was passed in the first quarter of 2013. So we're getting that credit this year in our provision, but we didn't have it in there last year.

Net income from continuing operations was $11.1 million for the quarter compared to $9.5 million for the second quarter of '12. That's a 17% increase. Earnings per share for the quarter related to continuing operations is $0.48, compared to $0.41 per share in the second quarter of '12. That's a 17% increase. The year-to-date net income from continuing operations is $24.3 million compared to $21.5 million for the year-to-date period in 2012, $2.7 million increase or 13%.

Diluted EPS for the year is $1.05 compared to diluted EPS for the 2012 period at $0.93. That's a 13% increase. On the bottom line, net income attributable to controlling interest is $11.1 million in the current quarter compared to the second quarter of 2012 at $10.4 million. That's a 7% increase and earnings per share related to those numbers is $0.48 for the second quarter of '13 compared to $0.45 for the second quarter of '12, a 7% increase.

In the year-to-date basis, net income attributable to controlling interest is $24.3 million in 2013 compared to $22.6 million in 2012, a $1.7 million increase or 7%. The diluted EPS related to those earnings is $1.05 on a year-to-date basis in the current year, compared to $0.98 on a year-to-date basis in 2012 for a 7% increase.

Our backlog—recall that we did sell American Augers in the fourth quarter of 2012 and therefore, we have adjusted the backlog in the prior year for the discontinued operations. Our backlog at June 30 of 2013 is $240.6 million compared to $254.8 million at the same date in the prior year. That's a decrease of $14.2 million or 6% decrease.

International backlog at June 30 '13 was $100.3 million, compared to $107.7 million at June 30 of '12. That's a $7.4 million decrease or a 7% decrease. Domestic backlog

PrecisionIR Group
9011 Arboretum Pkwy
Suite 295
North Chesterfield, VA
23236

Phone: 804-3273400
Fax: 804-327-7554

www.precisionir.com
www.investorcalendar.com
www.companyspotlight.com

this year at June 30 was $140.3 million compared to $147.1 million at June 30 of '12, $6.8 million decrease or a 5% decrease. Again backlog by segment is in your press release.

The balance sheet continues to be very strong. Our receivables are at $102.8 million at June 30 of '13, compared to $120 million at June 30 of '12. That's a $17.2 million decrease. However, $5.8 million of the decrease was due to American Augers at June 30 and so, the true decrease, if you were to take American Augers out the prior year's balance sheet, would be $11.4 million.

The days outstanding are down from 42.5 days outstanding at June 30 of '12, down to 37.3 days outstanding at June 30 of '13. Our inventory is at $318.7 million this year at June 30, compared to $322.1 million for a $3.4 million decrease, however we're moving American Augers again from the prior year number we gave you—an increase of $27.8 million year-over-year.

Inventory is at 2.3 turns this year compared to 2.5 turns in the prior year. We have nothing owed on our $100 million credit facility. We have $41.2 million in cash and cash equivalents. You'll notice that we do now have on the balance sheet in the press release an investments line item, that number has become material so we're disclosing that separately on the balance sheet. We did invest approximately $15 million of cash into some investments to get some yield on that, but you may wonder where some of the cash went. Well, it's in that line item. Also in the second quarter, we did pay our $0.10 per share quarterly dividend. That was about $2,285,000 paid out during the quarter on that dividend.

Letters of credit are sitting at about $10.6 million, so our borrowing availability is at $89.4 million. Second quarter 2013 capital expenditures are at $5.8 million and on a year-to-date basis we're at $15.2 million. We are projecting about $43.6 million of capital expenditures for the year. Depreciation is at $5.2 million for the quarter and $10.4 million on a year-to-date basis. We have budgeted about $22 million for the 2013 calendar year.

That concludes my remarks on the financial details. I'll turn it back over to Steve.

Stephen Anderson – VP of Administration, Director of IR and Secretary
Thank you, David. Don is going to provide some comments regarding our operations for the second quarter and he'll also offer some thoughts going forward. Don?

Don Brock – Chairman, Chief Executive Officer
During the quarter we continue to see flat revenues, as David said, with a slight 4% increase. Our earnings from continuing operations were up 17% and our earnings or EPS was up 17%. The strong dollar has negatively affected our international sales. We've experienced this year probably the wettest weather on record in the Eastern part of the country and especially in the Southeast. Here in Tennessee, we're 47 inches about a week ago and that's 17 inches above normal. This has delayed shipments of equipment and especially delayed our customers starting their work. Our earnings, although better in the second quarter, were negatively affected by higher health care cost, higher taxes from our Canadian subsidiary and from the GEFCO acquisition.

We see our customers remaining very cautious due to the uncertainty coming out of Washington. We find the market to be very competitive. Many customers on equipment are going from rent to rent instead of rent-to-own, and are demanding more as to rent more equipment than we've seen in the past. However, with all of

PrecisionIR Group
9011 Arboretum Pkwy
Suite 295
North Chesterfield, VA
23236

Phone: 804-3273400
Fax: 804-327-7554

www.precisionir.com
www.investorcalendar.com
www.companyspotlight.com

these negatives, we see residential and commercial work of our customers improving slightly. Each person that I talked to, or each customer says after a long pause, it's slightly better than it was last year. Not great, but it is improving.

We have begun to ship our first large pellet plant after a delay of approximately six weeks due to the rain. Our prospects are very good for this product and the market seems to be growing. We are in the process of merging Astec Underground into GEFCO and creating an energy group, eliminating the Underground group, as we've sold off all of the equipment related to that, that we manufactured.

Looking forward to the third quarter, we see the third quarter to be slightly weaker than the second quarter, but much stronger than third quarter last year. We believe sales of our new products and models will backfill the shortfall of our conventional products and should give us flat revenues even though the margins of these new products have not reached their desired peak that we hope to achieve. Our backlog is essentially flat from last year. We continue as we go forward, to work on margin improvement, but struggle with under absorption due to the lack of volume in most of our plants. Our parts business continues to grow. We see people replacing parts instead of replacing equipment.

As David said, our balance sheet remains strong and we continue to pursue acquisitions. We find them to be very competitive at this time. We continue to prepare for succession of myself and Norm Smith at year end. Ben Brock and Rick Doris are in the process of picking their replacements at Astec and Heatec. They are participating in our quarterly reviews and traveling to each subsidiary. We are pleased with the progress and look forward to the continuing growth of our company under this new leadership.

With that, I'll be glad to answer any questions. Ben is also on the call to answer any questions.

Operator
Our first question is coming from the line of Jack Kasprzak with BB&T Capital Markets.

<Q>: I wanted to ask you about the third quarter. I think I heard you say that revenues will be about flat and earnings will be less than Q2, but well above Q3 last year. On flat revenues, we're obviously thinking we're going to get a margin rebound in Q3 versus Q3 last year?

Don Brock – Chairman, Chief Executive Officer
Jack, our biggest problem is underabsorption in the plants. As you can see, our inventory has built up. We hope to reduce that a little bit during the third quarter. So the actual build schedule in the third quarter is probably going to be less, and it's not going to be indicative of the revenues. We have a lot of equipment delay due to weather so we'll be shipping it during the third quarter, but we won't be building as much as we built in the second quarter.

<Q>: The tax rates bounced around a little bit, and I was wondering if David had a view on where it will be for the full year?

David Silvious – Chief Financial Officer, Vice President and Treasurer
Yes, I think it will moderate back to our historical rate, 35.5%, 36% on a year-to-date basis.

PrecisionIR Group
9011 Arboretum Pkwy
Suite 295
North Chesterfield, VA
23236

Phone: 804-3273400
Fax: 804-327-7554

www.precisionir.com
www.investorcalendar.com
www.companyspotlight.com

<Q>: I was going to ask you about the Underground gross margin, but now you're merging it—you say you're merging with GEFCO and creating an energy group. Will that start as far as reporting like that in Q3?

Don Brock – Chairman, Chief Executive Officer
Year end, first quarter of next year, Jack. The margin should be fairly good in that group. We're building larger pieces of equipment. We're out of the smallest line, building pump trailers. We have two large, very large orders; one for $15 million and one for $8 million for vertical drilling rigs. We're pretty optimistic, I guess maybe a little more optimistic than backlog indicates, but our guys up there seem to think that the drill rigs, the pump trailers, the auxiliary equipment it goes with them is going to be a great product line and we seem to be on the leading edge in some of the things we're doing there.

<Q>: And for the full year, the press release mentioned maybe we get a little pickup in Q4 as the weather is cleared and projects get going, but that's only one quarter out of the whole year, sales are about flat. I mean, this year is shaping up to be about a flat year up slightly for revenue. Is that probably a reasonable assumption?

Don Brock – Chairman, Chief Executive Officer
Yes, I think that's right, Jack. The customers seem to have good backlogs, but a lot of it is just due to weather delays. I think they will be a little more optimistic. My discussion with most of them, as a lot of them had losses last year and they're probably not going to have losses this year, or they may not make much money, but they have delayed some purchases and I guess logically it tells me that they may buy a little more in the fourth quarter and in the first quarter of next year than they've been doing in the past. It's up a little bit but not up much.

Operator
Our next question is coming from the line of Rich Wesolowski of Sidoti & Company.

<Q>: If I recall in the Asphalt Group, you had raised product prices around year end and last call I think really very little inflation to purchase components. And I'm wondering if there's anything, aside from volume, that weighed on the group's June quarter margin?

Don Brock – Chairman, Chief Executive Officer
Ben, do you want to answer that?

Ben Brock – Vice President, Asphalt
Well, I would say that on the sales that we've taken in the second quarter that we've given a little bit of that price increase back, we had a couple of, well, one very large order that went into this next quarter and the Q3, but the orders have really kind of slowed down for us during Q2. So our hours worked or un-absorption was up and kind of got to us in the quarter.

<Q>: Is 100 basis points of company-wide gross margin expansion for 2013 still within reach or is the volume including that number?

Don Brock – Chairman, Chief Executive Officer
I would say that our gross margin is going to be about where it is right now. It doesn't look like it. We really saw a falloff in May and June and July, just saying slowdown and the underabsorption is what's really hurting us, Rich.

<Q>: You mentioned the six week delay because of the weather with regard to the pellet shipment. Are you still expecting to reach the performance target in 2013 or is that now moved to perhaps the March quarter?

Don Brock – Chairman, Chief Executive Officer
We are planning on it. It's going to be close.

Ben Brock – Vice President, Asphalt
Yes. What I would add to his rain comment is it's really tough in South Georgia. It's a flat piece of land and we're virtually going to be delivering as the concrete is curing and so it will really be, I hate to say, weather-dependent. We're going to do everything we can to be able to count that in Q4.

<Q>: Did the customer add on to the original plant order that you're now shipping?

Ben Brock – Vice President, Asphalt
Not yet. They're waiting on a sustainability legislation in the U.K. I was at a conference a week and a half ago and there was a lot of talk about that and the general feeling is that, that will get done before the end of September; that's talking with utilities, representatives and pellet suppliers that are working on the contracts. Their contract is essentially done, that would add the two lines to the current one-line plant, and once they get that supply contract signed, so they need the additional pellets for the next two lines, that would be what releases us on the next two. So we've been told by the customer to expect that by the end of September now.

Operator
Our next question is coming from the line of Mig Dobre with Robert W. Baird.

<Q>: This is Brian Brophy, in for Mig. Can you discuss what is giving you confidence that we'll see a pickup in demand in the fourth quarter as you mentioned in the release?

Don Brock – Chairman, Chief Executive Officer
Brian, I guess when customers have a decent year, they will turn loose of capital expenditures and I'm just going by gut feeling and talking to different ones that if they make money this year they'll probably spend a little. Their equipment is getting old and I guess that's what I'm counting on as much as anything. They have been delayed. They got a slow start due to the weather, but it's dried out now and there are a lot of people working, and there's pockets of prosperity.

One of our major customers in Georgia has as much work as he has ever had. He's a major contractor there. Virginia has a great program. They did away with the gas tax and put a sales tax on it, which raised a bunch more money, but the public didn't realize they were doing it. So that has a good program in Virginia. A number of states are looking at going to sales tax versus gas tax like Virginia. They're watching what happened there, but due to the backup in the work and the amount of work that they're doing, I'm saying they're going to finish the year stronger and probably have a better attitude, which will help their buying.

<Q>: Then can you provide us some additional color on your comments of customers seeing a slight pick up in residential and commercial work? Are we beginning to see some expansion in housing starts to new neighborhoods as opposed to housing starts in existing lots?

Don Brock – Chairman, Chief Executive Officer

PrecisionIR Group
9011 Arboretum Pkwy
Suite 295
North Chesterfield, VA
23236

Phone: 804-3273400
Fax: 804-327-7554

www.precisionir.com
www.investorcalendar.com
www.companyspotlight.com

PrecisionIR Group
9011 Arboretum Pkwy
Suite 295
North Chesterfield, VA
23236

Phone: 804-3273400
Fax: 804-327-7554

www.precisionir.com
www.investorcalendar.com
www.companyspotlight.com

To answer your question, yes, from what I'm seeing the housing starts obviously are up. They're kind of flat in the last month or so, but the size of the houses are smaller. They're not building as many big houses, but they are sucking up the subdivisions that were built before, and the commercial work has picked up. It's picked up from a very low level, but any of that work is at a better margin generally than the state work. So the state work or federal work is kind of flat and what was not there is at least there on the commercial and residential. I'm on the Board of a floor covering company and they're up like 25%, so the homebuilding is certainly helping.

<Q>: Then can you give us an update regarding the timing and the amount of revenue recognition for the first two Asphalt plants for the Army?

Ben Brock – Vice President, Asphalt
We're anticipating recognizing that in the third quarter. The testing, I think I referenced this on the last call, has not gone as quickly as we want it to go, but we're told that it will be finished this month and they're here. So we think that'll happen. So we do anticipate the first two plants being recognized this quarter.

<Q>: Ben, can you remind us what's in backlog, what the total opportunity is and what the risks for those orders is given sequestration?

Ben Brock – Vice President, Asphalt
Yes, we have five orders after these two that are in hand. Originally, they told us there would be eight. They say number eight is maybe a plant, maybe not, but we do have five, but they won't release us to build the next five until the testing is complete on these two, and there's a review that has to take place on that from Aberdeen. It should take anywhere from 30 to 90 days. We've been told probably in the 30-day range. We would love to be released on those five right now, because that would help us on underabsorption, but we're waiting on the Army right now. We're pushing them, but the Army is tough to push. It is five and those are firm, but we just don't have the release to build them.

Operator
The next question is coming from the line of Todd Vencil with Sterne Agee.

<Q>: Thinking about this weather impact a little bit and where it's going. I mean, do you have a number in your mind for how much revenue got sort of delayed on your end by the weather?

Don Brock – Chairman, Chief Executive Officer
My guess would be $15 million to $20 million. If you take the pellet plant, we would start shipping it earlier, but it wouldn't have been a complete shipment, but I would say $15 million to $20 million, in that range.

<Q>: If you talk to your customers, you mentioned, Dr. Brock, that things are starting to dry out. Are you hearing better color from them on the fact that they've been able to get up and go now?

Don Brock – Chairman, Chief Executive Officer
Yes. I mean most of them. I think July has been reasonably dry. Still a lot of rain, but they were able to work and most of them that I've talked to had pretty good late Junes and early Julys; they've had good weather here in the last six weeks.

<Q>: Are those customers feeling like they're going to be able to make up this year what they had delayed in 2Q, or is some of that going to get pushed into next year?

PrecisionIR Group
9011 Arboretum Pkwy
Suite 295
North Chesterfield, VA
23236

Phone: 804-3273400
Fax: 804-327-7554

www.precisionir.com
www.investorcalendar.com
www.companyspotlight.com

Don Brock – Chairman, Chief Executive Officer
I think most of it will be made up. The comments they made to me is they better get going or they won't make it up, but I think they have got going. I talked to one yesterday and he had a fantastic month in June. It's the first time he had made a profit in 15 months. So he was pretty excited and they have done a huge amount of work. A lot of them are actually running two shifts, running at night as well as the daytime so they can catch up. There's a lot of capacity out there.

<Q>: I guess this is for David. Thinking about that $7 million absorption variance, which is overall, I think, across all the segments, but mostly Asphalt and Aggregate mining. I mean if you haven't had the weather delays, would there have been a negative variance there or would it have been di minimis?

David Silvious – Chief Financial Officer, Vice President and Treasurer
I think it would have been less, but I don't think it would have gone away because even without the rain delays, there's still a little bit of a lack of hours that we're seeing.

<Q>: What does that absorption variance look like in the second quarter last year?

David Silvious – Chief Financial Officer, Vice President and Treasurer
Second quarter of last year was very small actually. It was actually close to break-even.

<Q>: So gross margin was flat year-over-year even though you had a $7 million, basically $7 million negative swing in the absorption variance?

Don Brock – Chairman, Chief Executive Officer
Right. We've made some improvements except for the underabsorption, and the problem we have too is we have a couple of companies that are over absorbed that are doing quite well in the Aggregate side of it. But in general, Asphalt has been slow and the aggregate companies that depend on international have been slow.

Ben Brock – Vice President, Asphalt
I would add to that, that we have adjusted our hours in the Asphalt Group, but it can change fairly quickly as orders come in that are time-dependent because jobs come up with the rain. So it also even in international where jobs get released and they wait to buy the plant until the last second. We picked up an order Friday night in Mexico that's a quick delivery, so all of a sudden we're going to adjust our hours again. It can turn fairly quick depending on how those jobs get released.

<Q>: Speaking with that in a minute, you mentioned product mix issue that contributed to the Asphalt margin coming in below where you thought it was going to be. What was that exactly?

Don Brock – Chairman, Chief Executive Officer
Generally going to the Tier 4 on the pavers and some of the new lines that we have, we still haven't recovered our margins to the point that we would like to have. A number of the new products we haven't reached our margin level that we will get to and that we historically have just not gotten there on the numbers of these new products.

<Q>: So as we think about the two big things you mentioned there in Asphalt the product mix, I appreciate that color and then the overhead absorption I mean, how are

PrecisionIR Group
9011 Arboretum Pkwy
Suite 295
North Chesterfield, VA
23236

Phone: 804-3273400
Fax: 804-327-7554

www.precisionir.com
www.investorcalendar.com
www.companyspotlight.com

you thinking about margins sort of coming out of this little bit of a swag there in the quarter. Actually what do you think about the next couple of quarters?

Don Brock – Chairman, Chief Executive Officer
We see margins continue to struggle due to the underabsorption and due to the new products. The new products are more in the Mobile Group and some in the Aggregate Group where we have the lowest margins that we have to recover from. In the Asphalt, it's strictly volume.

Operator
Our next question is coming from the line of Jason Ursaner with CJS Securities.

<Q>: Just a quick follow-up on the last question, I missed part of the beginning of the call. I apologize. Just looking at the Asphalt segment, revenue was down a little over $8 million sequentially and gross margin was also down a little over $8 million sequentially, so basically 100% flow through. That was all volume, there's no—I know last call you talked about legacy products, mix factor in Asphalt. I'm just trying to figure out how much specifically of that is absorption versus potential mix in Asphalt?

Ben Brock – Vice President, Asphalt
I would say, yes, mostly it is the volume. We have a couple of new products, one in particular we're working on how we recycle Asphalt plants where typically our plants would run—the double barrel would be a 50% wrap plant. We're having new design, we can go up to 70% or 75% and we have had some cost associated with that.

<Q>: In the Underground segment you guys had talked about a sizable project to Kazakhstan, just any update on that, on the delivery schedule and how revenue recognition and margin might work for that for project?

Don Brock – Chairman, Chief Executive Officer
It's probably going to ship in September. There is about half of that, that is basically purchased items that will not be typical margins and about half of it that we're building on that package. The one for Argentina, we'll be building more of the total package, but the Kazakhstan will be going out in September.

<Q>: And that would be when you recognize it also?

Don Brock – Chairman, Chief Executive Officer
Yes.

<Q>: And then also an underground, just an update on the GEFCO business. It still appears to be underperforming from a demand perspective relative to where it had been last year maybe at peak times, just maybe what the strategy is to grow the business?

Don Brock – Chairman, Chief Executive Officer
We kind of screwed up to be truthful. They were outsourcing a huge amount of their work, the machining, the machine tools when we bought that plant were1960s vintage. They were outsourcing all of the material prep and we brought in all of that work and we bought new machine tools and probably we did it too quickly. We're having to train people. They are getting up to speed. The material prep seems to be working well. The programming of the new machine tools is still a work in process. And as a result of bringing this sub work in quicker than we should have, we kind of screwed up their flow, to be truthful, and we are working our way out of that and should reduce our cost substantially when we get everything up and running. The end

PrecisionIR Group
9011 Arboretum Pkwy
Suite 295
North Chesterfield, VA
23236

Phone: 804-3273400
Fax: 804-327-7554

www.precisionir.com
www.investorcalendar.com
www.companyspotlight.com

of the third quarter should be better and the fourth quarter should be better. We have good backlogs there and we have good prospects there, but we rearranged the plant. It's a modern plant now, but we're just getting up to speed.

Operator
The next question is coming from the line of Ted Grace with Susquehanna Financial Group.

<Q>: Don, could you speak to the Highway Bill? We're about 14 months out from the expiration of the, call it 2.5-year mini Bill, just curious for what kind of insights you can share that are either, that you're picking up from the subcommittee level or the actual committee levels on both the house and the Senate side and kind of what your outlook is or expectations at this point?

Don Brock – Chairman, Chief Executive Officer
All of the politicians that our people talk to and I talk to recognize the need for highway spending. They all sit there and agree with you, but when you get to how you're going to pay for it, they just shut up and it's really frustrating. So we really just don't know. Ben, do you want to make any comments? I guess we're getting to the point that the contractors are beginning to get nervous about it. There'll be something, but God only knows what it will be. The problem with the present administration when they talk infrastructure, you better try to figure out what part of the infrastructure they're talking about too. It's not necessarily roads and bridges. I'm not giving you a very good answer, but we really, of all the times I've seen, don't see a lot of momentum on it.

Ben Brock – Vice President, Asphalt
I would agree with what he said. I had breakfast with customers this morning that are in town, and their state has done a lot of work, kind of like what you've mentioned with Virginia earlier or what you've heard about Virginia earlier, that it may be that the states end up long-term taking this over. But you don't have a lot of momentum for a Highway Bill. I know that the Asphalt Association out there had their mid-year meeting in Boston last week and I was up there at one of their legislative sessions and they're definitely focused in and starting to fly in. They seemed to be focused earlier, but I agree with Dr. Brock in that, there's not a how do you pay for it answer yet.

<Q>: So fair to interpret that as very much remains to be seen, but it sounds like certainly from your tone, you're not too optimistic that we'll get anything that's certainly bigger and the risk maybe skewed to the down side, would that be a fair interpretation?

Don Brock – Chairman, Chief Executive Officer
I'd be surprised if it's any bigger because we don't have the funding where it is right now, as you know, raises about $35 billion, and we're at $40 billion.

<Q>: The second thing I was hoping to dig into is, could you just update us on kind of how the mining industry is going within AMG, obviously the money markets are tough, cyclically speaking. You guys have kind of a different strategy and some update there would be helpful just to understand how that business is tracking versus expectations and what your thoughts are looking out for the next couple of years?

Don Brock – Chairman, Chief Executive Officer
I didn't quite get the question.

Stephen Anderson – VP of Administration, Director of IR and Secretary
He just wants an update on mining activity; how things are doing in the mining sector.

PrecisionIR Group
9011 Arboretum Pkwy
Suite 295
North Chesterfield, VA
23236

Phone: 804-3273400
Fax: 804-327-7554

www.precisionir.com
www.investorcalendar.com
www.companyspotlight.com

Don Brock – Chairman, Chief Executive Officer
Obviously with commodity prices going down, it slowed down the mining. We just completed our round of quarterly reviews and talking to our South African operation, gold and platinum, and a lot of those are down. Coal is up in South Africa. As we cut down on the coal in America these other countries are picking it up. But in general most of the mining projects have slowed down.

We have a pretty good size order from Australia for a mining project and I guess what we see is we're in more the processing side of it and there is a lot of replacement equipment. There is also a pretty good cattery of equipment that gets sold just to keep the leases and we have been such a small player in the mining side of it. We see a slight growth that for us at least in that even in a down market. But overall, I'm saying mining is going to be down the next couple of years.

<Q>: Would that be correctly calibrated to think that, that's kind of a 20% to 30% of revenue at AMG?

Ben Brock – Vice President, Asphalt
The mining.

Don Brock – Chairman, Chief Executive Officer
Yes, that would be about right.

Operator
Our next question is coming from the line of Morris Ajzenman with Griffin Securities.

<Q>: Just a follow-up back on the Asphalt Group, talking about the margins. We know that the Asphalt plants are kind of aged and you've talked about in the past weeks start to see a pickup of orders and you touched on sort of fourth quarter. I'm not sure with your previous answer this was in reference to that, but gross margins in this quarter 18.8%. If you do get a pickup in the order rate for Asphalt plants, I thought you had said that gross margins might be up some, I'm not really referring to Asphalt specifically, but my presumption would be if you had a pickup in the orders in Asphalt plants, why wouldn't you see a big step up in Asphalt gross margins?

Don Brock – Chairman, Chief Executive Officer
I guess it is product mix. We expect to get the other two lines of the pellet plant down in Georgia to build in the fourth quarter. We kind of expect the Army to release those five other plants. So we think we're going to build the plant back up. That's the biggest thing. Then we have a number of customers, potential orders for larger stationary plants that they're replacing older plants that they have told us they're going to do in the fourth quarter. They don't want to shut down during the middle of the year. We see prospects there that we feel fairly confident about getting, so I guess the three of those items; the pellet plant, the Army plants—the Army is not a great margin, but it puts an absorption, it help our absorption in the plant, and then we've got a number of prospects that are talking about fourth quarter orders, either fourth quarter or first quarter deliveries they want to be running next year.

<Q>: Alright, so and then as a follow-up again, the Asphalt group your target is a 25% gross margin for your divisions. The Asphalt Group, is that realistic then to see over the next four quarters at some point in time or will it take a lot longer than that to get to 25%?

Don Brock – Chairman, Chief Executive Officer

When you consider 25% of their business is parts, it helps to offset lower margins in the equipment and 25% may be a little rich, but 23% to 24% is probably reasonable.

<Q>: And one last question. Beyond the two lines for the pellet plants, are you in discussions with other end market utilities in Europe that would have an interest in stepping up and ordering these plants, anything in the discussion phase?

Ben Brock – Vice President, Asphalt
We are talking to a handful of customers. We're not talking directly to any utilities. Frankly, until the sustainability gets passed, everybody is getting quotes, but they are not absolutely serious until that point. I think the financing is held up by that too. But we are talking to a handful of other customers.

Operator
Our next question is coming from the line of Brian Rafn with Morgan Dempsey.

<Q>: Don, you spoke about some original strengths, some pockets of prosperity, you mentioned Georgia and Virginia. Are you seeing that pockets of prosperity expanding geographically or is that kind of static from your estimate?

Don Brock – Chairman, Chief Executive Officer
I think it's expanding. Some states like Iowa are doing better. I could go through—I don't know that I can through all 50 of them, but I would say that there's probably 20% better than it was a year ago. Even California is a little better; particularly more in Southern California than Northern. It seems to be doing better in the West. There's usually a wave that comes from the West to the East as things pick up and looking at where we're selling crushing equipment. Typically crushing equipment is a year ahead of Asphalt equipment and most of the customers that I talked to and in the crushing say it is up. I think statistics show it's only up about 4%, but I get the feeling that when the weather clears, it's probably going to be that the aggregate side of the business is going to be, I'm talking about our customers now, probably more like 15% or 20% year-over-year.

<Q>: Okay, give me a sense, with the under absorption issues and that, how does that and some sluggishness, you talked about confidence, how does that translate for you guys in developing and innovating new products? Does it force you to create more new product from the standpoint of differentiating or you kind of draw back a little because there just isn't that end market demand?

Don Brock – Chairman, Chief Executive Officer
We're taking a more aggressive approach to try to develop new products. If I look at the last ten years, if we hadn't developed new products, we would probably be doing half the volume we're doing today. In most of the companies, what we're building today, we didn't build ten years ago and it's a matter of survival is what it amounts to. If you don't continue to innovate, you're going to get left behind. I look at it more for survival right now. We did it for growth, but it's ended up being for the survival of the company. You have to continue to build new products.

<Q>: Yes, okay, okay. What, can you guys kind of give a ballpark on capacity utilization; you've talked about underabsorption on the Asphalt side, what might be running on a capacity utilization across your different groups?

Don Brock – Chairman, Chief Executive Officer
I would say it's probably less than 70% right now.

PrecisionIR Group
9011 Arboretum Pkwy
Suite 295
North Chesterfield, VA
23236

Phone: 804-3273400
Fax: 804-327-7554

www.precisionir.com
www.investorcalendar.com
www.companyspotlight.com

PrecisionIR Group
9011 Arboretum Pkwy
Suite 295
North Chesterfield, VA
23236

Phone: 804-3273400
Fax: 804-327-7554

www.precisionir.com
www.investorcalendar.com
www.companyspotlight.com

<Q>: How does that translate for you guys? There seems to be on the manufacturing side a lot of our shortage of engineers and that, how do you guys look, kind of based on your comments with innovating for survival, how do you look at headcount and hiring and staffing? Is that kind of flat for you guys or are you kind of episodically hiring or you're looking at headcount …?

Don Brock – Chairman, Chief Executive Officer
We're basically hiring to replace retirees and we're not really at this point trying to hire to grow because we just haven't been able to get the revenues. The growth in the last five years of our international certainly helped us in this downturn. The new products helped us in the downturn. But with international backing off and with the visibility not being too great, we're trying to remain cautious.

<Q>: You talked a little bit, Don, about guys, maybe the Asphalt side with obsolete equipment, aged equipment. At what point is there the ability to constantly just rent, rent ongoing or is there at some point a pent up demand to replace some of that in field obsolescence?

Don Brock – Chairman, Chief Executive Officer
It varies with the product. On an Asphalt plant, we certainly don't rent those, but crushing equipment, particularly track mounted equipment; they are more prone to rent to rent. We're seeing a lot of that; milling machines, mobile equipment. They like to do more rent to rent or at least rent to own. A lot of the larger customers are limited. They're people on CapEx, but they're getting the work and so they have no choice, but to rent to do the work. It comes about from that. On the Asphalt plant side of it, the need to change depends on the need to run higher recycle to be able to be competitive. The older plants you see I would say in a lot of areas of the country 30% or more of the plants are shut down, but they're old or obsolete plants that may never be cranked back up, because it wouldn't be very competitive because they can't run the higher recycle.

<Q>: Relative to the Army contract, are there any other demand for Asphalt across any of the other branches; Marines or Air Force?

Don Brock – Chairman, Chief Executive Officer
No, not a lot.

<Q>: Then you guys talked about tax rates. You got a CapEx budget for this year, 2013?

David Silvious – Chief Financial Officer, Vice President and Treasurer
Yes, we do. We mentioned that the CapEx budget for 2013 was at $43.6 million.

Don Brock – Chairman, Chief Executive Officer
A major part of that is building the plant in Brazil, and that's kind of a one-time item that's probably in the $10 million to $20 million, $25 million range.

Operator
Our next question is coming from the line of Rich Wesolowski of Sidoti & Company.

<Q>: With regard to the European incentives for biomass, I was under the impression that the utilities had already secured subsidies for burning wood and Ben had mentioned they're now waiting on something else, some other piece of legislation?

Ben Brock – Vice President, Asphalt

PrecisionIR Group
9011 Arboretum Pkwy
Suite 295
North Chesterfield, VA
23236

Phone: 804-3273400
Fax: 804-327-7554

www.precisionir.com
www.investorcalendar.com
www.companyspotlight.com

Yes, they do you have the floor price that they do have. The sustainability part is that for the environmental side of it, they want to make sure that all of the I's are dotted and T's ae crossed or everything is taken care of as far as where is the biomass or where is the wood coming from and are you replanting trees behind it. They have to have all of that legislation in place. That's part of the deal and they want to make sure that's reasonable, utilities and the suppliers of the pellets before they go ahead. You're right, the floor price is there. The utilities are happy with that, but that sustainability piece has to be finished before they all walk in.

Don Brock – Chairman, Chief Executive Officer
I think, Rich, the environmental groups started pushing back on it and the Parliament over there is trying to satisfy them, but they want you to be able to have a paper trail that shows that as you cut the wood, you're going to replant the wood, so that you have the zero carbon footprint.

<Q>: Right. Well from what I gather either way, they can't even sniff their larger renewables goals without the biomass, so it seems like a matter of time. You spent a lot of time talking about the market potential for the pellet plants, would you mind reminding us lastly the ways in which Astec plants specifically stand out from the competitors' versions?

Don Brock – Chairman, Chief Executive Officer
I think we have a very unique plant that we have a patents pending on and that we do indirect drying with the tube type dryer, rotary tube type dryer. As you dry, particularly southern pine or even hard wood, but pine generates a lot more VOCs. On a typical plant you have to put a, what they call an RTO where it's an active burner that would burn those VOCs up. In order to incinerate them, you have to heat it to about 1400 to 1600 degrees Fahrenheit. We are taking the VOCs off the rotary tube dryer and pulling them back through our thermal oil heater where we are heating the oil. So we're basically using the energy out of the VOCs to help heat the heat transfer that's in the tube dryer.

Our efficiency will be about 10% better from a drying cost and it basically is a safer type of operation. The biggest hot button I guess we have that the customers like, it is a modular plant. It's somewhat skid-mounted plant that if they run out of fiber at their, what they call the wood basket; they can pick it up and move it and not lose so much. They'll lose the concrete in the ground, but that's about it. The third thing is one substantial company offering a package. Right now, they're being put together by engineering procurement groups that buy a piece here, and buy a piece there, where we furnish the entire plan.

Operator
Our final question of the day is a follow-up question coming from the line of Todd Vencil with Sterne Agee.

<Q>: Real quick, SG&A was better … in the quarter and you mentioned that R&D was down again. What's the outlook for that and what kind of run rate should we be thinking about on SG&A?

Don Brock – Chairman, Chief Executive Officer
Pretty well what you have right now. Pretty well what second quarter was.

David Silvious – Chief Financial Officer, Vice President and Treasurer
That's right, Don. In the past, we have spent upwards of $8 million or $9 million the past couple of years in R&D. Our run rate over the past 10 years or so was in the

$4.5 million to $5 million. We're probably heading back toward that run rate, but we're still, right now, we're in the $7 million, $7.5 million range.

Operator
We have reached the end of our question and answer session. I would now like to turn the floor back over to Mr. Anderson for any concluding remarks.

Stephen Anderson – VP of Administration, Director of IR and Secretary
Thank you, Jesse. We appreciate everyone's participation on this Second Quarter Conference Call, and thank you for your interest in Astec. As our news release indicates, today's conference call has been recorded. A replay of the conference call will be available through August 6, 2013, and an archived webcast will be available for 90 days. The transcript will be available under the Investor Relations section of the Astec Industries website within the next seven days. All that information is contained in the news release that was sent out earlier today. This will conclude our call. Thank you, and have a good week.

Operator
Thank you. Ladies and gentlemen, this does conclude today's teleconference. You may disconnect your lines at this time. Thank you for your participation.

PrecisionIR Group
9011 Arboretum Pkwy
Suite 295
North Chesterfield, VA
23236

Phone: 804-3273400
Fax: 804-327-7554

www.precisionir.com
www.investorcalendar.com
www.companyspotlight.com