Transcript of Astec Industries, Inc.
Second Quarter 2016 Earnings Call
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Participants

Steve Anderson - VP, Director of IR
Ben Brock - President and CEO
Rick Dorris - EVP and COO
David Silvious – CFO

Analysts

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Mig Dobre - Robert W Baird
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Presentation

Operator
Greetings and welcome to the Astec Industries Second Quarter 2016 Earnings Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. [Operator Instructions] As a reminder, this conference is being recorded.

I would now like to turn the conference over to your host, Mr. Steve Anderson, Vice President, Director of Investor Relations. Thank you, you may begin.

Steve Anderson - VP, Director of IR
Thank you, Rob. Good morning and welcome to the Astec Industries' conference call for the second quarter that ended June 30, 2016. As Rob mentioned, I'm Steve Anderson, and also on today's call are Ben Brock, our President and Chief Executive Officer; Rick Dorris, Executive Vice President and Chief Operating Officer; and David Silvious, our Chief Financial Officer. In just a moment, I'll turn the call over to David to summarize our financial results and then to Ben to review our business activity during the second quarter.

Before we begin, I will remind you that our call 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 Private Securities Litigation Reform Act. Any such statements are not guarantees of future performance and are subject to certain risks, uncertainties and assumptions.

At this point, I will turn the call over to David to summarize our financial results for the second quarter. David?

David Silvious – CFO
Thanks, Steve. Thanks to each of you for being with us this morning. Net sales for the quarter were $294.4 million compared to $268 million in the second quarter of last year, an increase of 9.9% or $26.4 million increase in sales. International sales were $52.2 million this quarter compared to $72.4 million last year in Q2, a decrease of 28.9% or $21.2 million. International sales represented 17.7% of Q2 2016 sales compared to 27.4% of Q2 2015 sales.

The decrease in international sales compared to the second quarter of last year occurred primarily in Europe, Canada, Russia, Africa and Australia. And those decreases were offset by smaller increases in South America and Japan.

Domestic sales for the second quarter were $242.2 million compared to $194.6 million Q2 last year, a 24.5% increase or $47.6 million increase. Domestic sales were 82.3% of Q2 2016 sales compared to 72.6% of Q2 2015 sales.

Part sales for the second quarter were $63.8 million compared to $67.4 million in Q2 last year. That's 5.3% decrease or a $3.6 million decrease. Part sales were 21.7% of quarterly sales this quarter compared to 25.2% in Q2 of 2015. For the quarter, part sales increased in the infrastructure group and decreased in the aggregate mining and the energy groups.

Foreign exchange translation impact on sales was $3.4 million. That is to say that if rates this year were equal to last year's rates, our sales would have been $3.4 million higher.

On a year-to-date basis, sales were $573.1 million compared to $556.8 million for the first half last year; a 2.9% increase or $16.3 million increase. International sales were $96.7 million compared to $151.1 million first half last year, a decrease of 36% or $54.4 million.

The decrease year-over-year occurred in Canada, Australia, Africa, the Middle East, Europe and in the post-Soviet States and Russia. Those were offset by small increases in Japan and China.

International sales were 16.9% of our first half sales this year compared to 27.1% in the first half of 2015. For the year, international sales decreased across all of our reporting groups.

Domestic sales were $476.4 million in the first half of this year compared to $405.7 million in the first half last year, a $70.7 million increase or 17.4% increase. Domestic sales were $83.1% of total sales in the first half compared to 72.9% in the first half last year.

Part sales were $137.9 million compared to $140.5 million in the first half last year. That's decrease of 1.8% or $2.6 million. Part sales year-to-date were 24.1% of total sales compared to 25.2% of year-to-date total sales in 2015.

Foreign exchange translation on the year-to-date sales figures had a negative impact of $7.5 million. Again, that is rates were the same in this year versus last year, sales would have been $7.5 million higher.

Gross profit for the quarter was $73.4 million compared to $62.2 million in the second quarter of 2015, an 18.2% increase or $11.2 million increase. That made gross profit percentage 25% for the second quarter of 2016 versus 23.2% for the second quarter of 2015. One of the factors impacting net gross profit was the absorption variance for the second quarter of 2016, which was actually just about $100,000 dollars over absorbed whereas last year in the second quarter we were $2.4 million under absorbed, so that a $2.5 million improvement in efficiency in the shops.

Consolidated gross profit for the year was $145.4 million compared to $128.3 million last year for the first half. That's an increase of $17.1 million or a 13.3% increase in gross profit dollars. The gross profit percentage was 25.4% this year compared to 23% for the first half of last year.

The year-to-date 2016 absorption variance, we were under absorbed $1.4 million for the first half compared to last year's first half where we under absorbed $4.5 million. That's a $3.1 million positive change in the absorption variance year-over-year.

SGA&E for the quarter was $45 million or 15.3% of sales compared to $43.3 million or 16.2% of sales in the second quarter of 2015. That's a $1.7 million increase and a decrease of 90 basis points as a percent of sales. The factors impacting SGA&E quarter-over-quarter were primarily payroll and related expenses. That was increased $2.9 million, our exhibit expense was up $1.1 million, health and insurance expense was actually down $1.5 million, and IT and related consulting expenses was down about $1 million.

For the year, SGA&E was $88.8 million or 15.5% of sales compared to $87.1 million last year or 15.6% of sales. That's an increase of $1.7 million year-over-year and a decrease of 10 basis points as a percent of sales. Factors impacting those numbers in the year-over-year, payroll and related, about a $3.4 million increase, exhibit expense was about $1.8 million increase. Health insurance was down about $2.9 million, and IT and related consulting expenses were down $1.5 million.

Operating income then in the second quarter is $28.5 million compared to $18.9 million in the second quarter of 2015, a $9.6 million increase or a 50.8% increase in operating income quarter-over-quarter.

Other income in Q2 was $327,000 versus $420,000 in Q2 of 2015 and was $900,000 for the first half compared to $2.4 million for the first half of 2015. The primary source, as a reminder, is license fee income and investment income by our captive insurance company, but do recall that the prior year year-to-date number does include approximately $1.2 million of key main life insurance proceeds.

The effective tax rate for the quarter is 36.2% compared to 37.9% for Q2 2015 and 36.8% on a year-to-date basis versus 37.4% on a year-to-date basis in 2015. The things that impacted the tax rate for both the quarter and the year-to-date were the losses in our foreign jurisdictions for which we can't recognize a benefit and we had some higher state income tax expense at certain of our domestic subsidiaries.

Net income attributable to controlling interest was $18.2 million for the quarter compared to $11.8 million in the second quarter of 2015. That's $6.4 million increase or 54.2% increase.

Diluted EPS for the quarter was $0.79 compared to $0.51 for the second quarter of 2015. That's a $0.28 increase or 54.9% increase in EPS quarter-over-quarter.

Year-to-date, net income attributable to controlling interest $35.9 million compared to $26.9 million for the year-to-date 2015 period. That's a $9 million increase or a 33.5% increase and that was resulted in diluted EPS for the first half of 2016 of $1.55 compared to $1.16 for the first half of 2015, a $0.39 increase or 33.6% increase.

EBITDA for the second quarter was $34.6 million compared to $25.3 million for the Q2 of 2015, a $9.3 million increase or 36.8% increase. And for the year, EBITDA was $68.9 million this year compared to $55.4 million for the first half of last year, a $13.5 million increase or 24.4% increase in first-half EBITDA.

Our backlog at June 30 is $364.5 million compared to $229.5 million at June 30 last year. That's an increase of $135 million or 58.8%. International backlog was $54.5 million this year compared to $57.5 million at June 30, a decrease of $3 million or 5.2%. Domestic backlog was $310 million this year compared to $172 million at June 30 last year. That's a $138 million increase or an 80.2% increase.

The foreign currency translation impact on the backlog compared to June 30 last year, again, if rates were the same, was a decrease of $3.6 million. So, current year backlog would have been $3.6 million higher.

Our balance sheet continues to be very strong. Our receivables are sitting at $127.5 million compared to $118.2 million at June 30 last year, an increase of $9.3 million. Our days outstanding are 38.9 compared to 40.2 at June 30 last year.

Inventories at $379.5 compared to $382.8 million at June 30 last year, a decrease of $3.3 million. And our terms remained relatively flat at 2 terms compared to 2.1 last year.

We have nothing on our domestic credit facility of $100 million and we have $68.5 million in cash and cash equivalents on our balance sheet. Letters of Credit outstanding are $17.2 million. That's leaves us a borrowing availability on that credit line of $82.8 million.

We do have $10.6 million in debt in Brazil right now that's used to finance that company's buildings, building and furniture, fixtures and inventory. That's where the interest expenses are primarily derived from.

Capital expenditure for the quarter was $6.5 million and capital expenditures for the first half were $11.3 million. We're still forecasting around $30 million of capital expenditures for the year. Our depreciation is at $5.2 million for the quarter and $10.3 million for the year, and for 2016, the full year, we're forecasting about $22.5 million of depreciation.

So that concludes my prepared remarks, I will turn it back over to Steve.

Steve Anderson - VP, Director of IR
Thank you, David. Ben Brock will now provide some comments regarding the second quarter of this year's operations. Ben?

Ben Brock - President and CEO
Thank you, Steve. Thanks to everyone for being in our call today.

As we commented in our earnings release this morning, we were pleased with our second quarter results. While the headwinds of low oil and natural gas prices, the global mining slowdown and the strong US dollar persisted and challenged us in two of our three financial reporting groups during the quarter, we were able to secure and ship orders as a result of the passage of the federal highway bill in the United States, which allowed us to earn a good result in the quarter in our traditional business areas. We were also able to recognize $18 million in pellet plant revenue during the quarter.

As David mentioned, our earnings per share were $0.79 per share versus $0.51 per share in the second quarter of 2015, which was an increase of 54.9%. And our second quarter sales were $294.4 million versus $268 million, for an increase of 9.8%. Year-to-date sales are $573.1 million versus $556.8 million for an increase of 2.9%. And again, as David mentioned, our EBITDA year-to-date was $68.9 million versus $55.4 million.

EBITDA was up again in this quarter as our company's maintained stronger gross margin versus last year. Our product mix included more special project work than last quarter, so we were pleased with our team's efforts to keep gross margins in range with last quarter's gross margins. Higher capacity utilization rates in the infrastructure group and some of our aggregate group companies once again helped us on our gross margins.

Our backlog at June 30, 2016 was $364.4 million, which was up 58.8% versus last year. Our backlog remains strong mainly as a result of the $122.5 million pellet plant order that we announced during the first quarter. The pellet plant order backlog is in the infrastructure group backlog. Our infrastructure group also continued to do good order intake during the quarter mainly as a result of the federal highway bill in the United States.

Our aggregate mining group backlog was down due to the global mining industry being slow and delayed core investments in the United States. We have seen improved core activities since the first of July in this group and we believe the highway bill will help this group late this year.

Our energy group backlog was down primarily due to the price of oil and natural gas, as well as customer capital expenditures in those industries. Domestic backlog was up about 80% year-over-year and international backlog was down 5%. At the end of last quarter, our international sales were down 44.2% year-over-year which was near our trend for the full year of 2015, so we did experience some slight improvement on an international percentage basis.

The strong US dollar remains a significant headwind for our export efforts. International backlog remains down primarily due to the strength of the US dollar, of oil and natural gas prices and the global mining slowdown. Our Astec do Brasil facility continues to experience everything you read in Brazil with regards to the slow economic times and the political environment is not helping it out at all.

We continue to work for orders in surrounding countries to help fill this facility. We continue to hear from our infrastructure customers in the United States that they're experiencing good business levels. We also continue to pursue new business with new products in the United States and we are maintaining our international effort despite the challenges presented to us by the strong US dollar and depressed mining industries in our key markets. We are keeping our long view with regards to international and we do see a strong US dollar as oil prices and the mining conditions remaining in place for the balance of this year at the least. Our lower backlog in international is a direct result of those headwinds.

Our higher backlog in domestic was primarily due to the passage of long term federal highway bill in the US, good private sector work levels for our infrastructure customers and the pellet plant order we announced during the first quarter.

Changing subjects to the Hazlehurst, Georgia pellet plant, that's the original pellet plant that we shift that we have discussed on several calls. As a continual reminder, it's a new product that we chose to finance at the time. As a result, we will recognize the revenue for this plant as we are paid. This will have an effect on our cash and inventory until it's paid in full. The order for all three lines was for $60 million and we expect the final payment in 2017. As a reminder, the interest rate on the note is 6%.

We were pleased to report the $122.5 million pellet plant during the first quarter. And as a reminder, it's an add-on to the $30 million order that we recognized during the first quarter with Highland Pellets bringing in a total project order amount to $152.5 million. As we mentioned on our last call, our plan is to recognize the $122.5 million order as follows. During the second quarter we recognized $18 million, during the third quarter we would anticipate recognizing about $20 million, during the fourth quarter of about $35 million. The balance of the order, which is around the $45 to $50 million, will be recognized in 2017 as site work, installation and start-up are completed.

Updating our current pellet plant quote activity, we do have ongoing quote activity for new projects and we believe that we will have a new larger order late this year. We believe that that order will be in the range of $80 million. As a reminder, these deals are long and complicated to get across the line. While we are optimistic that a new project will happen by the end of this year, it could always be longer than we anticipate.

With regards to international sales overall, given the well-documented challenge globally, with regards to the US dollar strength, global mining and global economic environment overall, we believe that we will remain challenged for at least the rest of this year with regards to sales internationally. We remain committed to grow international sales over long-term and we'll continue to maintain our sales and service coverage around the globe.

On the energy side, we remain extremely challenged in our drilling and pumping equipment sales activity for oil and gas. We mentioned on our last call that we were going to move our street broom equipment line production to the most affected facility in Enid, Oklahoma. The line will keep its Roadtec brand name and will be sold and serviced by Roadtec. Demand for our brooms has been strong as we have released new models in the last year. We are happy to report that the first brooms have come off the production line and are successfully operating with customers in the field.

We have slightly offset sales challenges in heaters for oil and gas, and industries with sales to food processing and chemical plants. We have also continued to see reasonable sales of wood chippers and wood grinders.

Our concrete plants are built in the energy group and quoting activity remains good for these plants. We also have our first ready mix concrete plant set up in our yard at CEI in Albuquerque, New Mexico in testing phase bringing us to two of the nine planned concrete models. We have named this new plant the Fusion Plant. We remain optimistic on our outlook in the energy group in the long-term; however, barring an unexpected change in the majority of the markets we serve, we will be challenged in this group overall in 2016.

Looking ahead at the third quarter of 2016 and the balance of the year, we are encouraged by our backlog, our domestic sales outlook and our strong infrastructure group sales activity. Our new product development continues in all groups. In addition to our new Fusion Plant, we have our previously unannounced LTV 1100 material transfer vehicle built by Roadtec in field testing now. Designed and built here in Chattanooga, this machine will complement our industry-leading shuttle buggy line with a smaller, easier to move material transfer vehicle.

Regarding new products, next year is the ConExpo year. We spent around $4 million on the prior ConExpo and expect to be in that range for the upcoming ConExpo. We're also working on new products for this show, which will slightly increase our R&D for the balance of this year and into the first quarter of 2017.

Changing subjects to our outlook for the next quarter and the balance of the year, we believe that our third quarter of 2016 will be better than our third quarter of 2015. Our current revenue outlook for the balance of 2016 is up 5% to 8% versus last year with improved bottom line performance. As a reminder, our revenues are up 2.9% year-to-date versus last year and our profit is up 33.6%.

While our infrastructure group is performing very well, we are cautious on our outlook for the aggregate and mining group and energy group with the main headwinds for these groups being very real and persistent.

As mentioned in my earlier comments, from our last earnings release to now orders have been good in the infrastructure group since early December last year, mainly due to the highway bill in the United States. Orders are not strong internationally, mainly due to the strong US dollar and mining slowdown.

Energy group orders are soft for products targeted at the oil and gas industry. Aggregate and mining group orders are soft for products targeted at the mining industry. Product sponsor activity for us remain hot mix asphalt equipment sales both asphalt plants and mobile equipment, concrete plant quoting activity with pellet plant quoting activity and wood chippers and grinders quoting and sales activity.

Year-to-date part sales were down by 1.8% versus last year and were 24.1% of total sales versus 25.2% of sales in 2015. We remain committed to improving our part sales volume in the long-term along with working to increase competitive part sales. We continue to see results of our Lean effort helping us be a better company, and we continue to focus on our gross margins as well. These efforts played a part in our gross margins during the quarter.

Looking to the whole of 2016, we are optimistic that we will end the year ahead of 2015. The majority of our customers in the United States are experiencing a stable private market and we are focused on selling existing and new products. Given the headwinds we are facing, we are working to manage the businesses facing those headwinds to the market conditions where our business warrants. To that end, we did have staff and/or work hours reductions at the most affected divisions during the second quarter.

We mentioned on our last call that our goal is to add at least one company to our Astec family during 2016, so long as the company was both a cultural and strategic fit within the industries we serve. As most of you know, we were pleased to announce on July 7, 2016 that we signed an agreement to purchase Power Flame Incorporated for $43 million subject to final due diligence and any adjustments if necessary. Power Flame is located in Parsons, Kansas. They have been in business for over 50 years with Bill and Louise Weiner as owners for the last 37 years. Power Flame engineers sales and services burners for many industries including industrial and commercial uses. They are profitable and a successful business that we believe will add in the range of $40 million in revenues in 2017. They are a market share and technology leader in each segment that they serve.

Our Heatec and CEI subsidiaries buy approximately 200 burners per year from them for their thermal hot oil heaters. We are not a large customer for them as they build thousands of burners per year. They specialize in burners from 400,000 BTUs to 25 million BTUs but have built burners as large as 100 million BTU's. Our Astec subsidiary builds burners for asphalt plants from 20 million BTUs 20 million to 150 million BTUs, so we believe we have a good opportunity for technology transfer between divisions, particularly on the control side.

We believe that Power Flame has very good technology for low emission burners that we can learn from at Astec. We believe we can help Power Flame with our corporate purchasing agreements and benchmarking with our other companies. We are extremely pleased that Bill Wiener will remain with the company as President.

Power Flame will retain its name and location. They will join our energy group after the transaction is completed, which we are targeting for this third quarter.

In our full year revenue outlook of up 5% to 8% versus last year, we have included the anticipated revenue addition from Power Flame this year. One last thing on Power Flame I'd like to say is thank you to Bill and Louise Weiner for their working with us to get the agreement in place. They've built a great company with great team members and we are very fortunate to have a successful industry leader like Power Flame join our company.

Acquisitions remain a key piece of our growth strategy along with organic growth. We are still diligently working on potential acquisitions.

That ends my comments on the quarter and what's in front of us. Thank you again for taking the time to be on our call and for your support as we move ahead. I will now turn it back over to Steve Anderson.

Steve Anderson - VP, Director of IR
Thank you, Ben. Rob, if you would open the queue for questions, we'll be glad to take those now.

Question-and-Answer Session

Operator
Our first question comes from the line of Stanley Elliott with Stifel.

Q: Hey, guys. Good morning, congratulations and thank you for taking the call. Quick question, could you help us with the orders, when you are looking at the infrastructure business, how much of that business is book and ship in the quarter or otherwise could you help us frame that how long the typical lag is between booking and sales?

Ben Brock - President and CEO
This is Ben, Stanely, thanks for the comments on the quarter. On the infrastructure group, depending on the division, our backlogs are pretty strong, so some of those orders on asphalt plants potentially could ship in 2017 now. It's very active. We thought we would see a little bit of a slowdown in the summer when the bill came and we started getting orders because customers would be working, and they are definitely working, and I have seen a lot of customers during the quarter but the activity has remained fairly good through the summer. We got a large order last night on an asphalt plant. So, I would say that on the mobile side definitely could be in this quarter, late third-quarter to early fourth quarter on the asphalt plant would be shipping first quarter next year.

Q: Help us from an historical standpoint, once you have the highway bill or once we see on a multi-year bill, if my memory serves that you see really good trends for probably two to three years from the signing of a highway bill, am I correct in that assessment or maybe if you can help me out with that?

Ben Brock - President and CEO
You are correct. If you look at the funding, 2016 through 2020, and it depends on who is writing that number down but in general it is about $1 billion a year change from 2016 to 2017 and maybe close to $2 billion from 2017 to 2018. So the funding increases there and it's in place, which is nice. And it helps our customers psyche on spending money on larger CapEx and we're seeing it.

Q: Last one from me, on that $80 million potential wood pellet order, would there be opportunity for additional add-on, additional lines from that or does that seem to be pretty square?

Ben Brock - President and CEO
I think that one is pretty square, but I would say we're talking to probably as many as ten people with five of them being pretty serious. So, it's not the only one that we think can happen in the next 12 months or so. And we can deliver the whole 80 of that next one next year if it came soon enough, but it would have to be pretty close to the end of the year for us to do that.

Operator
Our next question comes from Mig Dobre with Robert W Baird. Please proceed with your question.

Q: Good morning, everyone and I guess I agree with the gentleman prior, this was a pretty nice quarter with very good margins. I guess, my question is I'm trying to flush out a little more as to what's going on in your infrastructure segment and I'm looking at your orders of call it $99 million, and these orders seem to be a little bit below what we've seen in the past six months in terms of core infrastructure orders, so excluding the wood pellet plants, and a little more in line with the order pace that we've seen in 2015 before the passage of the highway bill. So I guess I'm trying to understand here what's really going in the market and how you guys are thinking about the demand going forward in terms of not only just seasonal slowdown or acceleration, but really the sustainability of the bump in demand that we've seen after the highway bill passage?

Ben Brock - President and CEO

Thanks, Mig, this is Ben. Demand in the quoting activity I can just say is very strong. The plant that we got last night was a very large plant, it's an asphalt plant and it's pretty consistent. We have more customers coming in this week on our asphalt plant. And then on the analysis side, David has looked a little bit at the backlog, he may have a comment on it, but I feel really good about infrastructure side. The Roadtec backlog is very strong, but they may be picking up just a little bit of market share; we are transitioning there on the distribution side from west US to the east to a dealer model, which is really what that product should be sold through, and so we've been able to sign some Tier 1 dealers in the Northwest and California that we're very excited about. Well, more in California and the Rocky Mountains, not in the Northwest, I'm sorry. We had another dealer that we signed on that Agricon side in the Northwest and I'm sorry about that, but feeling really good about that. Got a Tier 1 dealer in Wisconsin, so I think for Roadtec the future is very bright.

David Silvious – CFO
Yes, Mig, this is David, just to give you a couple of numbers. On the backlog in the infrastructure group, if you take out all the pelletizer business out of that particular group and compare it to the prior year, we are talking about an increase of backlog of $81 million and that is about 175% increase without any pelletizer business. And I think as we have described back when the highway bill was in the process of being passed that we thought there would be an initial surge and then a bit of a lull and then picking back up. And again, there is seasonality built into where we are right now as well.

Q: Right. And I appreciate your comments, David. I guess, the nature of my question was really more along the lines of, I understand that your backlog is up, but it seems to me like the backlog was really up because of what happened in the fourth quarter and the first quarter, rather than what happened this quarter. And I don't mean to be splitting hairs here, but I'm trying to understand through demand versus seasonality, but I guess you answered that.

In terms of the back half of the year, can you kind of help us think through the way revenues would flow? And I appreciate the wood pellet detail, but should we expect revenues basically to be flat to up sequentially from the first half in infrastructure?

David Silvious – CFO
In infrastructure, it will be flattish. The third quarter is always the tough quarter, because people are working and we will have equipment that will creep in, in the fourth quarter, and the fourth quarter will be better than the third on the infrastructure side. And that will hold true probably through all our groups. It always seems like we're in, I hate to say, hand to hand combat during the third, but I mean the third always feels like it's a grind. But we do have good backlog coming into it and so I think it will be a better third than last year. I mean, we only made $0.10 a share last year in the third quarter and the year prior, we only made $0.08. So from $0.08 to $0.10, it'll probably look good on a percentage basis, but it still didn't make us feel very good and so we have an opportunity to be better in the third this year.

Q: Sure. And then maybe my last question, David, this one is for you, in terms of again in infrastructure, if that is kind of your revenue outlook or best guess for the back half of the year, how should we think about gross margin here, given your absorption dynamics? And also maybe if you can comment on raw material cost impact in the back half.

David Silvious – CFO
On the gross margin for the back half, I think you're going to see in that infrastructure group, it will be relatively flat.

Q: Flat year-over-year or sequentially?

David Silvious – CFO
Sequentially. They are operating at pretty good efficiency in that group right now and so taking more cost out of that process would be a challenge. Again, product mix has a lot to do with it, but as far as the gross margin goes, I'd say they are going to be pretty good going forward on the gross margin compared to where they are now.

Q: And material costs?

Ben Brock - President and CEO
Well, I believe I will talk about that here. This is Ben. The material costs, steel is the one that's the big one that everybody is watching. In the last three weeks, we've been to every single division physically in the North American side and the steel mills would like to raise steel 12% to 15% on us right now, but we're hedged, we're in pretty good shape through the end of the third, And then we're keeping a close eye on it and we'll see if we want to lock in in August, but we will have to adjust prices for what we see. We don't think it will be that high, but we think there will be some increase coming at us. Now, at the same time, we're doing a pretty good job on the purchase side on the other items, so we're in good shape for the moment with keeping an eye on August.

Q: Appreciate it, guys. Thanks.

Operator
The next question comes from Schon Williams with BB&T Capital Markets. Please proceed with your question.

Q: Hi, good morning. Just wanted to talk quickly on the financing for Power Flame, was most of that put on the revolver or you're going to pay part of it out of cash or?

David Silvious – CFO
It will be all cash. We had $68 million in the quarter, so it will be all cash.

Q: And margins on that business, are they equivalent to the corporate rates or energy segment?

David Silvious – CFO
Yes.

Q: All right. And then I wanted to talk about the timing of the second Highland shipment, you did $18 million this quarter, it was kind of slightly below the guidance last quarter of $20 million. I just wanted to just get a sense of how are things kind of ramping up, and I don't know, this may be related to the expansion that's going on in Chattanooga right now, can you just talk about kind of, as we get into kind of full ramp up mode on pellets through the rest of the year, do you feel pretty comfortable with the schedule that you put out there?

Ben Brock - President and CEO
We do, Schon. This is Ben. Part of it is percentage completion at site two, so the hiring we were in good shape on. So it could be that we are around $20 million. It depends on if it rains at the time of build in Arkansas or not, that can slow us down, but in talking with our guys last week, we're starting to see we've got some pretty good steam onsite. So we feel good about the schedule as it stands right now.

Q: All right, that's helpful. And then energy had a particularly good topline this quarter. I mean, sequentially, you don't see these kinds of pickups going into the spring. You do get to see more pickup, but this was quite robust. I'm just wondering, can you give a little bit more color, was there anything specific driving that and are those levels sustainable going forward?

Rick Dorris - EVP and COO

Schon, this is Rick Dorris. Heatec had a good second quarter; Peterson has had a good year so far and that continued in the second quarter. We started doing some fabrication for some of the other divisions at GEFCO, so that helps them a little bit; and CEI was about flat with last year, year-to-date.

Q: In CEI, I thought there was some expectation that maybe that would be picking up here?

Rick Dorris - EVP and COO
We do expect it to pick up for the second half.

Q: Okay. And that would be cement plants?

Rick Dorris - EVP and COO
Yes. Concrete plants.

Q: Okay. All right. And then maybe just one last one, if I may, I know you mentioned R&D picking up at some point. I'm just wondering maybe like the SG&A levels as we go into the back half and do you feel pretty comfortable with the $44 million, $45 million level or is there any kind of pluses or minuses we should be thinking of in the back half?

David Silvious – CFO
I think we're in a good place from SGA&E. If anything, I would hope we would come in with a little bit of a downside surprise on that, but we're working hard to hold that steady. And with the volume that we're running, there are additional costs, so we really target the percentage, we'd love to be at 15.

Q: Okay, great guys and congrats on the quarter.

Operator
Our next question comes from Morris Ajzenman with Griffin Securities. Please proceed with your question.

Q: Good morning, guys. First question, aggregate and mining, both on the revenue and on the backlog, can you give us some more granularity? Kind of breaking apart as best as you can aggregate from the mining group? And then secondly, a similar question, the energy group, if you can break apart energy from concrete, Heatec, etc., , if you could kind of give us some more granularity within each of those two divisions?

Ben Brock - President and CEO
Sure. Morris, this is Ben. Mining in the group typically might be 15% of the group, and where we are struggling is in South Africa, our Osborn Group is profitable but they're off. And then Brazil, as I mentioned on the call, is looking like a pretty tall mountain but we're going to be there when it turns around and it's an investment, we've got it sized down. Actually, we're slightly profitable in part of the quarter. And we're looking for other products that we can build in that facility, maybe not even just for Brazil, like we shipped an asphalt plant to Argentina, we have a few others quoted for out there, for around Brazil. So the Telsmith group's sales into mining a little bit as well, and they had a really soft first half but they've picked up. They have more work now, so it feels a lot better there.

On the energy side, right now the concrete is, we have the two plants going through right now that will go to a customer late this month or first couple of weeks of August, which is a fairly large order, around $7 million altogether, so that will show up with CEI. That alone can help them in their second half. They would meet that criteria immediately on concrete plants. But they have pretty good work otherwise, and they've picked up a few asphalt type orders and asphalt rubber blending type prospects. But right now, I'd say concrete is not significant. Next year, for CEI, $10 million to $20 million range would be pretty achievable. I know that's a wide range, but they are coming in new to the industry.

And Fusion Plant that is referenced in my comments is a smaller ready mix plant. It's a fairly simple process with newer style controls, and those retail in the neighborhood of $450,000. So we are not talking it's going to take a lot of units to move that needle for the company, but for them it would move it a lot. It would be good man-hours and a lot of work. I hope that answers your question. That's kind of where we are on it.

Q: Just as a follow-on back with the agri and mining, can you give us a little more discussion on the aggregate side of the business, where we were in the quarter and how it looks going forward?

Ben Brock - President and CEO
On the portable and track mounted side, it's stayed steady, flat, but still steady. And the project work, the larger quarry work has lagged. We were hoping it would be quicker but like we said on the last call, we now think, and in my comments today, back half of the year or probably near the end of the year for the highway bill to help that group. It's just come out of the gate a little slower with the highway bill then we would like. But good quoting activity there now since the 1st July. We haven't earned the orders yet, but at least we've got more quoting activity. Actually, we have had some orders at Telsmith, but it feels a little better now than it did 25 days ago.

Q: Last question, I don't think it had any major impact for you, but BREXIT at the end of June, have you seen any fallout or any rebound or any impact at all from that?

Ben Brock - President and CEO
No, we haven't seen any impact at all. We're keeping an eye on the labor side for our Telestack Group in Northern Ireland, which is in the UK. We talked with them within the last couple of weeks about it and there was not an over concern about anything for them. So the other concern for us when that happened was the pellet business, of course, because most of the driver for that business right now is the UK. Talking with our customers, that are doing business there, they do not think that it will affect what they are doing.

Q: Thank you.

Operator
Our next question comes from William Bremer with Maxim Group. Please proceed with your question.

Q: Good morning, Ben, David and Stephen. Just want to get a sense on overall pricing, I'm not sure if you gave a little commentary on that as of yet now, and couple that with your capacity utilization of your plants, is it necessary, given what we're seeing in steel, to start anteing up the price or is it based upon capacity utilization that you are able to possibly increase prices here?

Ben Brock - President and CEO
Bill, I'm sorry, this is Ben. We mentioned just a little bit ago that we're watching steel for sure, and we may need to think about pricing in August or early September, but for sure we'll be watching that hard. All of our purchasing managers are on red alert watching that because that's a big thing for us.

Utilization is good. Overall, it's up a little, we were saying 70, 75 last time. I'd say we're probably in the 75 range now as a company overall, with infrastructure running 80 plus, aggregate and mining running in the 70/75 range, depending on the group, and energy at around 65.

It's interesting. We've been very fortunate, but you can feel as good as you can feel in Chattanooga, Tennessee with our infrastructure group companies here, Astec, Heatec and Roadtec; you can feel maybe not as good, if you go to GEFCO, in Enid, Oklahoma that's been in the oil and gas business and water well business, which is flat to down a little. But we've been able to backfill some of the man-hours through the shop and the quality of work that they're doing is very good. So that's encouraging.

But we're definitely watching steel prices and I would say we talked about that last call, having just a little bit of pricing power, I think I've talked about putting your thumb and your index finger almost touching and that was it. I think you can probably still have them together, but you could probably take them out about a millimeter. So we have a little pricing power but we're still seeing very competitive markets. We faced the international competition with where the euro is from Germany, they are pretty aggressive.

Q: My next question is based upon just demands. Are there certain regions or states that you're surprised of in terms of their underlying demand for your products?

Ben Brock - President and CEO
Without giving too much away competitively, I would say we have activity coast to coast and we have pretty strong activity in the Southeast United States. That could partially be because our coverage is typically better closer to home, just because we started here, but we have good activity coast to coast.

Q: And northern, so our friends in Canada, what are you seeing there at this time?

Ben Brock - President and CEO
We have pretty good activity up there for quoting. I don't know if they are getting comfortable with the currency where it is, but it's more east than west; quiet in Alberta, that really depends on oil sands, but we do have generally pretty good activity right now in Canada. Hopefully, the sales will follow, but the activity is good.

Q: Okay, thank you, gentlemen.

Operator
Our next question comes from Mike Shlisky with Seaport Global. Please proceed with your question.

Q: Good morning, guys. Nice quarter. Ben, your commentary, assuming it was not positive around the oil and gas industry and that segment in general, but could you really tell us if you're seeing conditions improve or perhaps worsen over the last two months and so last year?

Ben Brock - President and CEO
I think they are about the same. We have quoted some equipment, which is encouraging, because in the first part of the year, I'm not sure we were even quoting it. I'll ask Rick to comment, he's closer to GEFCO and the quotes.

Rick Dorris - EVP and COO
Yes. The quoting activity has picked up some, but mainly in the water well part of their business. That part of their business has picked up in the last couple of months and there is a little more activity there. Oil was still down, but a little better than it was.

Q: Okay, got it. I also wanted to follow up on the last question earlier about your capacity utilization. So it looks like here you are running about 80% of your infrastructure. Can you give us a sense as to your capacity up to 100% and whether you have the ability to add on additional capacity at some point, given the pretty strong orders you're seeing?

Ben Brock - President and CEO
Yes. This is Ben, Mike. I would not anticipate 100%. There is just always going to be some underlying inefficiencies and when we do work on the shop, 100% is probably, it would be a great goal, but probably

unrealistic. I think in our best ever we've probably been 90%. And I think depending on the division in the infrastructure group, we might be getting closer to that, we are adding on at Astec, Inc. I would say they're probably pushing that number. We're adding on for drums, the drums for the asphalt plants that do the drying of aggregate and the drums that did the drying of the wood that they were building will handle the big drums for the drying of the wood and it's also set up to build drums for asphalt plants and that's our bottleneck. And we think between that and a couple of things we've done on our Dillman division, we can handle the demand that's coming at us out at the moment on the asphalt plants.

Q: Okay. And just on the same line with asphalt plants, a while back you had mentioned that your order activity could actually be close to building backlog that you did in December, then it will be followed by some kind of lull eventually. I was wondering, I thought it was going to be somewhere around Q2, which just took place, but what happened in Q2, which was actually very, very good, count as your lull? Or is that still yet to come or is it just not going to happen based on what's been going on recently in the asphalt market?

Ben Brock - President and CEO
Well, I think the quoting activity lulled a little bit but the quote to order kind of stayed fairly consistent on the plants, which was obviously a nice surprise. If you're going to be wrong, that's the right way to be wrong, I guess. But the quoting activity slowed as the summer came, but we've just been fortunate to be talking to people that were ready to do something and that's been great. Now, the challenge of that is, to the point earlier is, we've had some people take them later to stay with us, which has been great, but at some point, so far, I think there has been one deal that I'm aware of that we lost due to the delivery since December that they had to get in on, they had to start.

Q: Yes. I think that was the other question I had for this particular segment was, is there the opportunity, is there a chance that some of your customers just won't be able to wait as long as you've got? Of course, you are one of the market leaders, of course, but is there a chance that you might have some cancellations in your backlog at some point if the orders keeping on coming in and the demand is actually stronger than you initially thought?

Ben Brock - President and CEO
I don't think anybody will be canceling out of our backlog on hand, but we might not get orders because they've got a project that they didn't anticipate getting that they need a plant for really quick, like an 8- to 10-week delivery and we're dead in the water here with that. That potentially can happen. If DOTs come out with quick mill and inlay work for the end of the year, that could happen. That being said, we'll do all we can to see if we can get there, we'll call everybody to see if we could do it. We wouldn't just lay down, but that's possible, because we are also not going to lie to a customer on delivery, we just can't do that.

Q: Of course, sure. Got it. Maybe if I can squeeze in one last one here on the pellet plant quoting activity, you've got some new ones. You mentioned one was in the $80 million range. I assume that that's a smaller plant than what you've currently got in the backlog. I guess maybe you can update us on the pricing and margin outlooks on for what you're quoting. Is it similar to the $120 million you have now or is it better or worse?

Ben Brock - President and CEO
That's a smaller plant; that is the plant that's going to— I keep going between my head Time Bluff and Hazlehurst. Time Bluff is a four line plant and we have all the install, so that's a big difference in the number between Hazlehurst Time Bluff, even though Hazlehurst is a three line and Time Bluff is a four line. That big spread is insulation freight, all the electrical that a lot of stuff that Hazlehurst would have self-performed. But this one is a two line plant where we have all-in, everything, site work and everything, I think I'm remembering it right. So that's more than just the iron. In fact, it also has wood yard in it, which is more equipment that we might outsource, but we're handling as an install on the equipment.

Q: Okay, sure. Got it. I will leave it there. Thanks, guys.

Operator
Our next question comes from Nick Coppola with Thompson Research Group. Please proceed with your question.

Q: Hi, good morning. For wood pellets, can you just talk more about kind of at a high-level your expectations for demand there, so beyond that next order that you just got, what are you looking at? Maybe into 2017, what are your thoughts around demand?

Ben Brock - President and CEO
This is Ben, with whom we are talking with, 1 to 1.5 of these plants in 2017 is our goal and what we're working for. We would love to have it sooner than later, so we can balance demand and keep openings for our asphalt plants. But our goal would be in the $100 million to $125 million range of revenue in 2017 with pellet plants.

Q: Okay, that's helpful. And then can you just talk more about Power Flame and how that fits into your portfolio of businesses from a strategic perspective?

Ben Brock - President and CEO
This is Ben, and they are a company that we've known for a long time. I've known them, we purchased from them when I was at CEI, I went out there when I was 26 and I'm 45 now. It's hard for me to admit that. So I've known them a long time, known their culture. Then when you look at strategically what they bring, being in burners for that long and we build burners, we can trade ideas on the burners, we can get more familiar with the industries they serve and there are places where their burners go on boilers and things that we potentially could see for other industrial applications for our growth. Some of the industries they go into that might tie in to some of the energy group companies or into the bio industries, they give us visibility into those industries that we don't have, being in all the things that they are in.

We can help them we think with purchasing and benchmarking, because they have a broader view of other companies that are doing similar things. I think between the two companies on the burners, so as mentioned earlier in my comments, the low emissions and being able to collaborate on that and some of the industries that they are in internationally, they do quite a bit of business in China and Russia, and some of those industries we can get a look into for some of our industrial equipment as well.

We're not necessarily, wouldn't get too excited about becoming competitors to our customers in the boiler business or that type of thing, but getting around what those go into might have some interest to us from the industrial side for growth in the energy group.

Q: Okay, that's very helpful. Thanks for taking my questions.

Operator
Our next question comes from Brian Sponheimer with Gabelli & Company. Please proceed with your question.

Q: Hi, good morning, guys. Thanks for fitting me in after 11 o clock here. Just on the original plant that you financed, what remains for you to get paid on the $60 million?

David Silvious – CFO
Quite a bit. Well, so they are working out their banking plan, just getting the financing. So what we have to do is we have to complete the retrofit and installation of one particular line, all three lines up and running, which two of them are at their current design, which is the final design. So that first line needs to be retrofitted. Once that

occurs, all three up and running according to spec and then the banks are all in. So it's a matter of timing more than anything.

Q: Okay. So of the original $60, you mentioned $20 million in the quarter, so $40 million remains, is that still?

David Silvious – CFO
Totally different project.

Ben Brock - President and CEO
Yeah. The $18 that we recognized in the quarter was on the Highland Pellet project, so there is almost all the $60 that's due, I mean, that we still have financed with Hazlehurst. And more color on that, all three lines have run pellets at production. What we needed to do is be able to burn wood exclusively on each line and we hit a wall on that on our burners, so we're replacing the burners. So the testing, proving that the lines will do what we said on tons per hour is fine. The other two have the new burners on, they are running. We have to put the third burner in, but they could get financing on that plant without it and that's the rest of the story.

I want to make sure everybody understands, we're not in a jam and at risk or anything, because there is no risk. We have met that and we are in good shape. But as far as how much money do we still have to collect, we have collected a little interest, but we were just thinking about it internally, it is about $60 million plus the interest.

Q: And just on the Highland plant, that's just percentage of construction there?

Ben Brock - President and CEO
That's right. Yes.

David Silvious – CFO
And that financing is in place and it's just a matter of completing the various terms of the contract.

Q: Thank you very much.

Operator
Our next question comes from Ryan Hamilton with Morgan Dempsey Capital Management. Please proceed with your question.

Q: Good morning, guys. Most of my questions have already been answered. I just like to touch real quick on the infrastructure group, could you talk a little bit about what you're seeing as far as your customers adding capacity or are they just filling orders as needed?

Ben Brock - President and CEO
It is a mixture, Ryan. This is Ben. We've had some customers adding plants to their fleet, but we also have had consolidation of plants for bigger plants. So we've sold some mega plants, what I call mega plants that would do 500 tons an hour plus and have 6 to 9 storage silos on them. There has been quite a few mega plants sold this year. But the used market is strong and so we've seen, as we've traded and sold and helped broker some plants, they are not staying on the market very long either. And then we've had some people that were not in the business get in the business, and so we've seen a couple of plant orders that have shipped this year that have gone to customers that were not in the plant business, but they were in the laydown business; they had pavers to pave asphalt. So it's a fairly active market for three of those reasons.

Q: Sure. Thanks for the color. And then I was kind of wondering if you could talk about being that it's been so long since we've had such a straightforward highway bill, I forget how many extensions over the last eight or so years, is this happening as you would expect it to happen or are there things that are coming up that you say, wow, this is different or unique?

Ben Brock - President and CEO
No, I think it's been about what we expected with the exception of being fairly consistent on the buying side, even though the quoting went down. It may be that we're still down on the orders side, it just seems like it's more consistent through the summer. There was a mid-year asphalt association meeting a few weeks ago that we were able to spend a day and a half in and generally the attitudes are very, very good.

Q: Okay, great. Well, thanks again and great quarter.

Operator
Ladies and gentlemen, we've reached the end of our question-and-answer session. And I'd like to turn the call back to Mr. Steve Anderson for closing comments.

Steve Anderson - VP, Director of IR
Thank you, Rob and everyone. We appreciate your participation on the second quarter conference call. 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 9 and an archived webcast will be available for 90 days. A transcript will be available under the Investor Relations section of the Astec Industry's website within the next seven days. All of that information is contained in the news release that we sent out earlier today. As Rob said, this concludes our call. So thank you and have a good week.

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