Transcript of
Astec Industries Inc.
Third Quarter 2016 Earnings Call
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Participants
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Rick Dorris - EVP & COO
David Silvious - CFO

Analysts
Stanley Elliott - Stifel
Mig Dobre - Robert W. Baird
Jordan Bender – Seaport Global
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Wayne Pinsent – Gabelli Funds
Brian Rafn – Morgan Dempsey

Presentation

Operator
Greetings and welcome to Astec Industries' Third Quarter 2016 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.

I would now like to turn the conference over to Steve Anderson. Thank you, you may begin.

Steve Anderson - VP, Administration & Director, IR
Thank you, Brenda. Good morning and welcome to the Astec Industries' call for the third quarter that ended September 30th. My name is Steve Anderson, as Brenda noted, and I am the Vice President of Administration and Director of Investor Relations for the company. 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 third quarter.

Before I 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 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'll turn the call over to David to summarize our third quarter results. David?

David Silvious - CFO
Thanks, Steve, good morning, everybody, glad you're with us this morning. Our net sales for the quarter were $247.8 million compared to $211.4 million in Q3 of 2015, that's a 17.2% increase in sales or $36.4 million

increase. International sales were $47.9 million in the quarter compared to $55 million last year in Q3, that's a decrease of 12.9% or $7.1 million decrease in international sales.

International sales represented 19.3% of this year's Q3 sales compared to 26% of last year's Q3 sales. The decrease in international sales for the third quarter compared to the same quarter last year, primarily in Canada, Africa, and in South America. These decreases were offset by some increases in Australia, Central America, and in the West Indies.

Domestic sales for the third quarter were $199.9 million compared to $156.3 million Q3 2015, for an increase of 27.9% or $43.6 million increase in domestic sales. Those domestic sales were 80.7% of our Q3 2016 sales compared to 74% for Q3 of last year. Part sales for the third quarter were $63.1 million compared to $62 million for Q3 of 2015, that's an increase of 1.8% or $1.1 million increase in part sales. Those part sales were 25.5% of our Q3 quarterly sales compared to 29.3% for Q3 of 2015. For the quarter, part sales increased in the energy group and in the infrastructure group, and decreased in the Ag and mining group.

Foreign exchange translation on sales had a negative impact of $2 million, and that is that if rates this year were the same as rates last year, sales would have comparatively been $2 million higher. Net sales year-to-date were $820.9 million compared to $768.1 million for the first nine months of last year, that's a 6.9% increase or $52.8 million increase.

International sales for that period this year were $144.6 million compared to $206.1 million for the first nine months last year to 29.8% decrease or $61.5 million decrease. The decrease on a year-to-date basis year-over-year was primarily in Canada, Africa, the Middle East, South America and in Europe. Those decreases were offset by small increases in Southeast Asia and in China.

International sales represented 17.6% of net sales for the year-to-date period this year compared to 26.8% for the year-to-date period in 2015. For the year international sales decreased in each of our groups.

Domestic sales were $676.3 million compared to $562 million for the first nine months last year, an increase of $114.3 million or 20.3%. Year-to-date, those domestic sales were 82.4% of 2016's year-to-date sales, compared to 73.2% of year-to-date sales in 2015.

Part sales for the year-to-date period were $201 million compared to $202.5 million in the prior year, that is a decrease of 0.8% or $1.5 million decrease in part sales year-over-year. Part sales for the year-to-date 2016 period were 24.5% of total sales compared to 26.4% of total sales for the year-to-date period in 2015.

The foreign exchange translation again had a negative impact on sales for 2016 of $9.5 million that is, that if rates were the same this year compared to last year, sales would have been comparatively $9.5 million higher.

Gross profit for the quarter was $55.4 million compared to $45.1 million in the third quarter of 2015 at 22.7% increase or $10.3 million increase. Gross profit percentage was 22.4% for the third quarter compared to 21.4% in Q3 of 2015. Our absorption variance for the third quarter of this year was $6 million of unabsorbed overhead; that compares to $5.4 million of unabsorbed overhead in the third quarter last year. So we did have a negative change in absorption variance of $600,000 quarter-over-quarter.

Gross profit on year-to-date basis was $200.8 million compared to $173.4 million; that's a $27.4 million increase or 15.8% increase. Gross profit percentage as a result was 24.5% for this year-to-date period compared to 22.6% for year-to-date 2015. The absorption variance on a year-to-date basis was $7.5 million of unabsorbed overhead compared to $9.9 million unabsorbed overhead in 2015; that is a $2.4 million positive change in absorption variance year-to-date versus year-to-date.

SGA&E for the quarter was $44 million or 17.7% of sales compared to $41 million or 19.4% of sales in Q3 of 2015; that's a $3 million increase in dollar terms but a decrease of 170 basis points as a percent of sales. The primary drivers in the increase, were payroll and related expenses, some profit share expenses and research and development. Those were offset by repairs and maintenance expense decrease. Remember last year we had a major repair on an aircraft engine that we had to take and we did not have that again this year.

For the year-to-date we had $132.7 million of SGA&E or 16.2% of sales compared to $128.1 million of SGA&E in the prior year or 16.7% of sales; that's a $4.6 million increase on a year-to-date basis or a 50 basis point decrease as a percent of sales on a year-to-date basis. Again, the primary drivers of the dollar increase were payroll and related expenses, profit share expenses, and we had exhibit expenses earlier in the year. We offset those increases with decreases in health insurance expense, and again as previously mentioned the repairs and maintenance expense that was incurred last year but not this year. We believe that the Q4 run-rate for SGA&E will be in that $43 million range.

Operating income in the third quarter was $11.4 million compared to $4.1 million for Q3 of 2015; that's an increase of $7.3 million or 178% increase in income from operations quarter-over-quarter. Year-to-date operating income was $68.1 million compared to $45.3 million in the year-to-date period last year, an increase of $22.8 million or 50.3% increase.

Interest expense again was $264,000 for the quarter compared to $505,000 last year and $1,057,000 for the year-to-date compared to $1,222,000 in the prior year. Remember that the primary driver of interest expense for us is currently the debt that we have in Brazil. We are financing their plant, their equipment and property and inventory down there. Although the debt is down, down there from September 30 of 2015, it was $8 million last year, at this time it's down to $6.9 million this year.

Other income was $508,000 for the quarter compared to $844,000 last year, and $1.4 million for the year-to-date compared to $3.2 million for the year-to-date period last year. The primary source of other income for us is license fee income and investment income at our captive insurance company. The year-to-date prior amount also includes key man life insurance proceeds of approximately $1.2 million.

The effective tax rate for the quarter was 41.5% compared to 52.5% in the prior year, and for the year is 37.6% compared to 38.8% for the year-to-date period last year. Now the effective rates for the quarter and the year-to-date were impacted primarily by increasing a portion that's domestically in the high tax rates states along with higher rates in those non-combined filing states, and we also had losses at certain subsidiaries for which the company could not recognize the tax benefit. Those things contributed to the effective rates being higher than the statutory rates.

Net income attributable to controlling interest for the quarter was $6.8 million compared to $2.3 million in the third quarter last year; it's an increase of $4.5 million or 195.7% increase in net income. Diluted earnings for the quarter was $0.30 compared to $0.10 in the same quarter last year, an increase of $0.20 or a 200% increase in EPS quarter-over-quarter.

Year-to-date, our net income was $42.8 million compared to $29.2 million in the year-to-date period last year, an increase of $13.6 million or 46.6% increase. And the EPS for the year-to-date period is $1.85 compared to $1.26 in the same period last year, a $0.59 increase or 46.8% increase.

EBITDA for the quarter was $18.1 million compared to $10.8 million for the quarter last year, a $7.3 million or 68.2% increase. And for the year-to-date EBITDA is $87 million compared to $66.1 million for the year-to-date period last year, a $20.9 million increase or 31.6% increase.

Our backlog at September 30 is $389.3 million compared to September 30 last year of $251.8 million. Remember that the prior year of backlog is adjusted for our acquisition of Power Flame, which occurred on August 1 of this year, so you do have a true apples-to-apples comparison there.

That increase in backlog is $137.5 million or 54.6%. The international backlog this year is $63.7 million compared to $58.7 million at September 30 of last year; that's an increase of $5 million or 8.6%. Our domestic backlog this year is $325.6 million compared to $193.1 million at September 30 of last year, a $132.4 million increase or 68.6% increase.

The September 30 backlog of $389.3 million compares to the June 30 backlog of $364.5 million, so sequentially we are up $24.8 million or 6.8% up in backlog sequentially. The foreign currency translation impact on the backlog was minimal, it was about $900,000.

Our balance sheet remains very strong. Our receivables are at a $111.8 million compared to $105.2 million this time last year, a $6.6 million increase. But our days outstanding are down. They are at 40.8 days outstanding compared to 45.9 last year.

Our inventories at $399.7 million compared to $384.5 million at this time last year, a $15.2 million increase. Our terms remain flat at about two terms this year and last year. We owe nothing on our $100 million domestic credit facility, and we have $52.5 million in cash and cash equivalents on the balance sheet. Letters of credit outstanding are $15.2 million leaving us borrowing availability of $84.8 million. If you recall, we previously mentioned we do have $6.9 million of debt currently in Brazil used to finance that company's building, fixtures and inventory.

Our capital expenditures for the quarter are $7.6 million. And year-to-date we're at $19 million and for 2016 we think we're going to end up around $23 million of CapEx. Our depreciation for the quarter was $5.2 million and our year-to-date depreciation is $15.5 million, and we believe that we'll end up 2016 somewhere in the $21 million range on depreciation.

So that concludes my prepared remarks on the financials. I'm going to turn it back over to Steve Anderson.

Steve Anderson - VP, Administration & Director, IR
Thank you, David. At this time Ben Brock will provide some comments regarding the third quarter of this year's operations. Ben?

Ben Brock - President & CEO
Thank you, Steve, and thank you to everyone for joining us on our call today. As we commented in our earnings release this morning, we were pleased with our third quarter results. While the ever persistent headwinds will blow yet stabilizing oil and natural gas prices, the global mining industry glut and the strong US dollar continue to present challenges to us, we continue 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 for the quarter in our traditional business areas.

We were also able to recognize $19 million in pellet plant revenue during the quarter. Earnings per share for the quarter were $0.30 per share versus $0.10 per share in the same quarter last year for an increase of 200%. Our third quarter sales were $247.7 million versus $211.4 million last year for an increase of 17.2%. And our year-to-date sales were $828.8 million versus $768.1 million for an increase of 6.9%. And again as David mentioned our year-to-date EBITDA was $87 million versus $66.1 million for an increase of $20.9 million in EBITDA on a $52.7 million increase in sales.

EBITDA is up again this quarter as our company has maintained stronger gross margins versus last year. Our major product mix was fairly normal this quarter. Our higher capacity utilization rate and infrastructure group once again helped our gross margins. Our backlog at September 30th was $389.2 million up 54.6% versus last year. Our backlog remained strong partially as a result of the $122.5 million pellet plant where we announced during the first quarter this year the pellet plant order. Our backlog is in the infrastructure group backlog.

Our infrastructure group also continued 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 quarry investments in the United States. We have seen improved domestic quote and order activity in this group since October 1st and we believe the highway bill will help this group as we move in to next year.

Our energy group backlog was up slightly as products targeted and infrastructure customers gained some momentum and power plants backlog joined the group as well. Domestic backlog was up about 68.6% year-over-year and international backlog was up 8.6%. Our higher backlog and domestic was primarily due to the passage of the long-term federal highway bill, good product sector work levels for our infrastructure customers and the pellet plant order that we just discussed a minute ago.

Regarding our increase in international backlog, we mentioned in our last call that we experienced slight improvement in international on a percentage basis during the second quarter. Given that our backlog in international was up for the first time in a long while versus the prior year quarter, we are encouraged to say that we have seen a slight improvement once again. Our increase in backlog in international was a direct result of pent up demand and our team executing where we could for orders.

Despite our gains internationally, the strong US dollar remains a significant headwind for our export efforts from the United States based operations. International backlog remains down historically, primarily due to the strength of the dollar, low oil and national gas prices and the global mining slowdown. Our Astec do Brasil facility continues to experience everything you read about Brazil with regards to slow economic times. We are committed to this facility for the long-term, and we will be in a good position when conditions improve in Brazil, however in the meantime we continue to pursue work for this facility in countries that surround Brazil.

We are maintaining our international effort despite the challenges presented to us by the strong dollar and the press mining industries in our key markets. While we are keeping our long view with regards to international, we do see a strong US dollar, flat oil prices and flat mining conditions remaining in place for the foreseeable future.

Changing subjects to the Hazelhurst Georgia pellet plant that we have discussed on several calls as a continuing reminder it was a new product that we chose to finance. As a result we'll recognize the revenue for this plant as we are paid. This will have an effect on our cash and our inventory until it's paid in full. The order for all three lines was for $60 million; 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 order during the first quarter this year, it is an add-on to the $30 million order that we recognized during the first quarter with Highland Pellets, bringing the 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. In the second quarter about $20 million and it ended up at about $18 million, in the third quarter about $20 million and it ended up about $19 million, and in the fourth quarter about $35 million for a total of approximately $105 million in 2016, with the balance of the order being recognized in 2017 in the range of $45 million to $50 million. That's the site work, installation and start up.

I was able to visit the Highland site a few weeks ago and I'm happy to report that the site looks great and the project is on-schedule. We anticipate starting line one in November.

Updating our current pellet plant quote activity, we do have ongoing quote activity for new projects, and we believe that we will add a new large order late this year or early next year for delivery in 2017. We believe the order will be in the range of $50 million rather than the $80 million we mentioned on our last call. We're also working on new projects that are in the $100 million range each. Based on what we know today we project that our pellet plan revenues will be in the range of $100 million to $125 million in 2017. This includes the remaining $45 million to $50 million that we anticipate from the Highland Pellets project.

This projection does not include the $60 million Hazlehurst wood pellet plant. Assuming we are paid on Hazlehurst in 2017, it would be in addition to our projection, however, as mentioned on prior calls we would only breakeven on the revenue. As a reminder these deals are long and complicated to get across the line.

While we are optimistic that a new project will happen in the timeframe mentioned, it could always be longer than we anticipate.

Changing subjects to the energy group, we remain extremely challenged in our drilling and pumping equipment sales activity. We continue to increase our street broom equipment line production in Enid, Oklahoma at our most effective facility in the energy group. The line remains a Roadtec brand name line and it is sold and serviced by Roadtec.

We have slightly offset sales challenges in heaters for oil and natural gas industries, with sales of asphalt terminal systems during the quarter. Sales of wood chippers and grinders remain consistent during the quarter, and our concrete plants that are built in the energy group, we have very good quoting activity.

We mentioned in our last call that we had our first ready-mix concrete plant set up on our yard at CEI testing which brought us to two of non-plant concrete plant models completed. As a reminder, we named this new plant the Fusion plant. We are pleased to announce that we have sold this plant. We remain optimistic on our outlook in our energy group, in the long term, however, barring an unexpected change in some of the key markets we serve we will be challenged in this group overall for the rest of this year and at least during the first half of 2017.

Our new product development continues in all groups, in addition to our energy groups and the Fusion plant that we have sold, our aggregate and mining group completed engineering and manufacturer of a new flexible production modular crushing system. Jointly designed by our JCI and KPI subsidiaries, this new system will have the flexibility to provide cone-crushers for 200, 300 or 400 tons per hour production rate, while being able to be easily shipped in standard shipping containers. We're happy to report that this system was not only built during the third quarter, it was also just sold.

Regarding new products, the ConExpo trade show starts just 133 days from today. We spent around $4.2 million on the prior ConExpo and expect to be in that range for the upcoming ConExpo. We have been 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 2017.

Looking ahead to the fourth quarter of this year, 2016, we are encouraged by our backlog, our domestic sales outlook and our strong infrastructure group sales activity. Giving these encouraging signs we believe that our fourth quarter this year will be better than our fourth quarter last year. Our current revenue outlook for the full year 2016 is up between 6% and 9% versus last year, with improved bottom line performance.

As a reminder our revenues are up 6.9% year-to-date versus last year, and our profit is up 47.1%. While our infrastructure group is performing very well, we are cautiously optimistic on our outlook for aggregate and mining group and cautious on outlook for the energy group, with the main headwinds for this group being very real and very persistent.

From my last earnings release to now, orders have been good in the infrastructure group mainly due to the highway bill. Orders are slightly better internationally, however 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 that improved for products targeted at the infrastructure customers. Aggregate and mining group orders are soft for the products targeted at the mining industry. Bright spots for activity are hot-mix asphalt equipment sales, asphalt plants and mobile type equipment, concrete plant quoting activity, wood plant quoting activity, wood chippers and grinders, and international quote activity despite the strong dollar.

For competitive reasons we will not be indicating the regions of activity, however we do feel the responsibility to indicate that our quote levels have increased internationally. Year-to-date part sales were down by just under 1% versus last year and were 24.5% of sales versus 26.4% of sales in 2015. This represents an improvement from last quarter's result. We remain committed to improving our part sales growing in the long term along with working to increase competitive part sales and service 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. These efforts played a part in our gross margins increasing quarter-over-quarter.

The majority of our customers in the United States are experiencing a stable private market, and we are focused in selling existing and new products. Given the headwinds we are facing, we are working to manage the business in the market conditions where the business warrants. To that end, we did have staff and/or work hour reductions at our most effective divisions during the quarter.

As most of you know we were pleased to announce on July 7th that we signed the agreement to purchase Power Flame Incorporated for $43 million, subject to final due diligence and any adjustments if necessary. As we announced this deal closed on August 1st, and they were accreted to us during the quarter. Power Flame engineer sales and services burners for many industries including industrial and commercial uses. They are a profitable and successful business that we believe will add in the range of $40 million in revenue in 2017.

They are a market share and technology leader in each segment that they serve. Our Heatec and CEI subsidiaries do buy approximately 200 burners per year from them, for there thermal hot oil heaters; however we're not large costumers for them, as they build thousands of burners per year. They specialize in burners from 400,000 BTU to 25 million BTU but have built up to over 100 million BTU burners.

Our Astec subsidiary built burners from 20 million BTU to 150 million BTU. So we believe we have good opportunities for technology transfer between the divisions particularly on our control side. We believe that Power Flame has very good technology for low emission burners that we can learn from at Astec. We believe that we can help Power Flame with our corporate purchasing agreements and benchmarking with our other subsidiaries.

And we have already found purchasing benefits not only Astec Company Power Flame, that's Power Flame helping Astec. We were pleased that Bill Wiener will remain with the company as president. As a reminder Power Flame retained its name and its location, and they have joined our energy group reporting group.

In our full year revenue outlook up between 6% and 9% versus last year we have included the anticipated revenue and addition from Power Flame this year.

With regards to the energy group, we were proud to add a new group president of the energy group during the quarter. His name is Jaco van der Merwe. Jaco comes to us from Atlas Copco. Jaco was with Atlas Copco for over 18 years in progressive roles that included some global responsibilities. Rick Dorris, our COO, was previously providing oversight at the energy group, in addition to his role as COO. The addition of Jaco to our team will free Rick up to fully focus on his COO duties.

Speaking ahead to 2017, we are optimistic with regards to our infrastructure group's outlook on infrastructure related equipment. We are cautiously optimistic on wood pellet plants in this group. We believe our aggregate and mining group will be up slightly next year, and we believe that our energy group will improve on the bottom line in 2017 despite the challenges we face.

Taking all that together, we will have the opportunity to successfully grow and operationally improve our company for the fourth year in a row in 2017.

In closing, 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'll now turn it over to Steve Anderson.

Steve Anderson - VP, Administration & Director, IR
Thank you, Ben. Brenda, if you'd open the queue, we'd be glad to take questions.

Operator
Our first question comes from a line of Stanley Elliott with Stifel. Please go ahead with your questions.

Q: Hi, guys, good morning, thanks for taking my question. Quick question, could you talk about the cadence and the deceleration sequentially in the infrastructure group from Q2 to Q3? Is all of that your typical seasonality? Is some of that the wood pellet coming out? Just kind of help us reconcile that move.

And then along those lines you mentioned the negative variance on the absorption in the quarter, if you could go through that in there, too.

Ben Brock - President & CEO
Hi, Stanley, this is Ben. On the volume side, the third quarter for us is always, I hate to say hand-to-hand combat, but it sure feels like that, and then you have some that don't make it across the line like if you have terms of over the rail for international shipping for instance. We had one that was over the rail for the ship wasn't disconnected from the port. And sometimes we run into that and third quarter is always a bear. Although I would say that it sure feels a lot better this third quarter than the last two third quarters because we were really struggling in the last two third quarters. So, it feels a lot better, but yes we had a few of those this time.

David Silvious - CFO
Stanley, on the unabsorbed overhead piece of that, the increase there occurred primarily in the Ag and mining group. There was a little bit of a slow down there, primarily related to mining, it was not necessarily on the Ag side, but mostly related to the mining side.

Q: Could you give us an update on the capacity expansion that you all had put out? Was that happened this quarter, or was that going to happen November if you can refresh our memory with that?

Ben Brock - President & CEO

This is Ben again, we originally planned to be fully operating in the middle of October. We are building some equipment in the new bay at Astec Inc. but it's not fully operational. That's probably a couple weeks away, quicker if we get lucky, but the building is finished. It looks great but we need more iron in there.

Q: And then lastly, you mentioned the Hazelhurst piece, and you threw out the word assumed it would get paid for in 2017. Is that really a question or is it really more just the timing as to when we can expect that revenue to fall into 2017?

Ben Brock - President & CEO
I used a bad word there. I feel like we're getting paid in 2017, I just didn't put it in the projection because there's not profit in it, and I was afraid if we put it in that big projection, and if we had margin in it and as people ran their models, we'd all get tangled up. We get paid but there's not really profit in it. It's not a loss either. We're maintaining it at a breakeven.

Q: So we'll be at a breakeven level into next year.

Ben Brock - President & CEO
Yes.

Q: Thanks guys, best of luck.

Operator
Our next question comes from the line of Mig Dobre with Baird. Please go ahead with your questions.

Q: Good morning, guys. I want to maybe go back to Stanley's first point in the infrastructure group about the sequential revenue decline. And if I'm looking sequentially what happens here seasonally, you do have a decline but it seems like this year is a little more pronounced than what I've seen in prior years, even though it doesn't look like you had that big of a shift from the second to the third quarter in terms of realized revenues on the wood pellet plants. So I guess my question is this. Do you have capacity constraints at this point and that's what's sort of causing this sequential revenue movement, or is there something else?

Ben Brock - President & CEO
Hi, Mig, this is Ben. No, we're okay on capacity. I think the other thing thinking about the question some more Australia and Germany are in that group as well. And they did not have great quarters and I think that affected it a little bit. That's more US dollar related. Although I would tell you that we have a little bit of a heartbeat on Australia, which is great, and Germany's got a few things going. They're in the right places, hopefully we can get some of these things across the line very soon.

Q: Okay, then maybe I can ask this differently. In terms of your capacity utilization within this group, where are you now versus I don't know what you would consider normal and this addition of a new production bay, what does that do exactly for your capacity going forward?

Ben Brock - President & CEO
So in the infrastructure group on the asphalt plant side, we're running 80% to 85%, probably the same on the mobile equipment side. And we have moved some of that production for delivery issues to our GEFCO facility; we've built some asphalt equipment there.

To my knowledge, and I had breakfast with some of our sales guys, we got them in here today for some training, we've lost one plant on pure delivery reasons and that was to a nontraditional Astec customer. If we had delivery 50/50 we could have gotten it. Now, it could be a challenge to us in the next few months but we have to get this bay open. We can do some shift work at one of our facilities to help that, and we are adding people in Chattanooga and we are able to get people. It's taking a little bit longer but the people that we're getting are good people, so we feel okay about our ability to deliver in this market.

Q: Okay. And then, I don't know maybe coming out of the last call last quarter, my understanding was that you guys were really thinking here in the infrastructure business that you're going to have to back half revenue and margin, largely gross margin, that is largely similar to the front half. Now maybe I'd misunderstood the way you tried to communicate that, but when I'm looking at the third quarter and the way you're talking about the fourth quarter, there seems to be a bit of a delta here. And I'm trying to reconcile that in the back of my mind like what is different versus what you originally expected and how do we think about gross margin in infrastructure going forward.

Ben Brock - President & CEO
Well, I think gross margin in the fourth quarter we'll have more pellet plant volume. As we build more lines, we're getting better at those margins, so they're now in the high side of our normal quoted margin. So I think you can think of it as gross margins in the infrastructure group in the range of what we saw earlier this year in the fourth quarter.

Q: And in terms of revenue out of your backlog, because we're talking 200 and call it almost $90 million worth of backlog, what's your visibility as to what you get, what you are able to convert in the fourth quarter?

Ben Brock - President & CEO
We don't give revenue guidance on that. So I would just say that we feel pretty good about having a good fourth quarter.

Q: This my last question. I'm asking this because I think if you look at this quarter, this is where the big variance was and I'm trying to make sure that we all have our models straight for fourth quarter, given what's coming out of your backlog. Can you help us at all as to the fourth quarter versus the first half or versus the third quarter, however you want to put it?

Ben Brock - President & CEO
Mig, we just don't give revenue guidance. I'm not sure we can really answer. I would love to tell you what we think our sales, net income and gross margins exactly would be, we just don't give that guidance. It should be better than last year's fourth quarter.

Q: Okay. It was worth a try. Thank you.

Operator
Our next question comes from the line of Mike Shlisky from Seaport Global. Please go ahead with your questions.

Q: Good morning, this is Jordan Bender on for Mike Shlisky this morning. My first question is that your cash levels remain quite high even after the Power Flame deal. You mentioned in your prepared remarks, you're working on acquisitions. Can you give us an update on any potential cash use through the first half of the year? Thanks.

Ben Brock - President & CEO
This is Ben. We're active on the acquisition front and we would like to use cash toward acquisitions that are in what we do. So we're energy, aggregate and mining and infrastructure industries. If that's our city I've always said we want to stay in our metro area, and everything that we're looking at is in that. We're not looking to load

up on a lot of debt. We are not going to set the house on anything, but there are opportunities for us and it's interesting how that works. We've looked at a lot that we haven't moved on but we want to have a cultural fit with whatever we do and so we're active on that. So we would pull the trigger for the right one.

Q: Got it. I'm going to throw one more in here. Could you comment on the upcoming election cycle, without giving us any type of endorsement either way? Could you maybe give us your thoughts on what a presidency and Congress with the same party controlling both sides, if that were to happen either party, what would it mean for potential increases to infrastructure and highway spending?

Ben Brock - President & CEO
Sure, both candidates seem to be good for infrastructure. Hillary Clinton has said on the record, $275 billion over five years, and Donald Trump has said $500 billion with really no timeframe tied to it. So while getting into the politics, I would love to, but we won't. They both sound good for infrastructure. And infrastructure when you look at stimulus, every president seems to want a stimulus package in their first year. There's not a whole lot to go into that well and pull out for stimulus so thankfully, infrastructure is usually bipartisan.

And so we feel good that either one of them, even at discounted numbers on top of the current highway bill would be good for us. And I would only add to that, thank goodness we have a highway bill in place while all this craziness in the election is going on. I think if it wasn't it would be a total lockdown for our customers.

So we've been very fortunate to have a highway bill in place while these two candidates really embarrass us all globally. So that's what I would say about that. They both sound pretty good, even at a discounted number after it gets through the Congress.

Q: All right, I appreciate the color.

Operator
Our next question comes from the line of Nick Coppola with Thompson Research. Please proceed with your questions.

Q: Hi, good morning.

Ben Brock - President & CEO
Good morning.

Q: So I just wanted to ask about how the FAST Act has been flowing through your business, and it sounds like the aggregate side of aggregate and mining has seen a longer lag than the asphalt plant and the infrastructure group. Maybe help us think about that and your expectations for quarry type equipment as dollars turn into construction projects.

Ben Brock - President & CEO
Sure, Nick. This is Ben. I think part of the weakness that we identified earlier on the aggregate group a lot of that was at Telsmith, who traditionally focuses on the big quarry projects and those just didn't come out of the gate as strong as the other onsite crushing and open shaft type crushing. But they've picked up, they have some work and we think that's a result of the highway money coming through the system. It always takes a little while for that money to come through the system.

I've been staying in touch with customers and last week was with a few of them, and they're not sure that the private wasn't really what was pushing it. And now they're seeing the state money coming through on the ones that I was with. So I think it's just been a delayed reaction, but based on the quote activity and the sales activity at Telsmith we think that is starting to show up.

Q: On the asphalt side, how would you characterize the impact, I mean it sounds that's already—

Ben Brock - President & CEO
I do think it affected the buying decisions earlier than it did on the quarry side because we've just seen pretty consistent activity there and better activity through the summer than normal when they're working. We talked about when it first started we thought there'd be a two month run when there was a bill signed and maybe a lull as people figured out what's happening and then it would kind of kick back in for maybe two or three years. And what we saw was that though we had the two month run it just stayed better through the summer as far as activity, instead of now, we're in the buying season and there's quite a bit of activity.

Q: Okay. Thank you for taking my questions.

Operator
Our next question comes from the line of Wayne Pinsent with Gabelli Funds. Please go ahead with your questions.

Q: Hi guys, congrats on the fabulous gross margin in the quarter. You touched on infrastructure gross margin earlier but can you tell any expectations of where overall margins could end up in the current quarter versus Q3?

Ben Brock - President & CEO
Hi, Wayne, this is Ben. It should be better. We have good utilization and we have little more work to cover up some hours in the aggregate group. When we started this with the highway bill, and looking back historically, in the 25 to 26 range was the high side. I guess we've pushed 26 on the high side. I think we can get back in that range during this cycle. We've already kind of went over it when we were really loaded up and things just kind of hit. But I think 25 to 26 in this 2- to 3-year cycle is a target we need to be trying to hit as we have this volume.

Q: And do you have any anticipation of when you would hit the high side of the cycle?

Ben Brock - President & CEO
Well, we touched it, we've already been in the 26 range as we started. We have a highway bill in place that is going to help our business we believe for two to three years and if we can get oil and gas to make a comeback a little bit, mining to comeback just a little bit, we have an opportunity to maintain that a little bit here for a couple of years.

Q: All right, thank you very much.

Operator
Thank you and we have follow-up questions from the line of Mig Dobre with Baird. Please go ahead with your questions.

Q: Yes, thanks for taking my follow up. Just clean up question on energy. Can you remind us what the Power Flame contribution to revenue in orders were in the quarter?

David Silvious - CFO
Revenue for the quarter was in the \$5 million to \$6 million range at the bottom of August 1st, recall that. And then from a backlog standpoint, the contribution to backlog was \$3.5 million.

Q: In backlog?

David Silvious - CFO
At September 30 of this year, and in the backlog of last year, just so you know it was $6 million because we did adjust prior year's backlog. So recall that.

Q: Got you. And I'm sorry, the $3.5 million versus the $6 million, I'm trying to equate that. Is that their own backlog declining to that extent or is it that you're recognizing partial quarter or something like that? How do I reconcile those two numbers?

David Silvious - CFO
Those were orders in place at the end of the month.

Q: Got it and then last question I know we talked about this a little bit in the past but I'm wondering if you can give us an update on raw material costs, fuel prices have been volatile. At what point do you start to see some impact from higher steel prices? Is it a fourth quarter? Is it next year?

Ben Brock - President & CEO
Hi, Mig, it's Ben. Last quarter we were getting indications that the steel mills and all their suppliers wanted 12% to 15%, and we saw some steel pricing increase at a couple of divisions, and it affected them slightly but not much. They really haven't been able to get the increase. And we have had a couple of notices, actually today, of people trying again but we're doing a little buying ahead now, using the hedge is a wrong word. We assume longer term buying right now. It's still relatively pretty good.

That being said we've met with all our presidents in person, the last week of August, and absolutely harped on watching cost in steel and pricing because if that moves on us, as everybody knows, that's a big deal so our presidents, we are on top of it.

Q: But should I understand that this is not really a concern for you or a material headwind to margin going forward?

Ben Brock - President & CEO
Not right now. Not for us.

Q: Okay. Thank you.

Operator
Our next question comes from the line of Brian Rafn with Morgan Dempsey. Please proceed with your questions.

Q: Good morning, guys.

Ben Brock - President & CEO
Good morning.

Q: Give me a sense, you talked a little bit, Ben, about the pent-up demand with some of the road builders. Can you put any more flavor in demand say from a national design build contractor versus maybe sales, how robust sales are at the regional or the local levels? Some of the smaller contractors.

Ben Brock - President & CEO

Sure, Brian. It's an interesting question because I'm just lucky because I asked that question last week. And what it is, in the asphalt plant side, over 95% of what's happened with our order since December 1st of last year has with privately-held companies. So that means that most of our business with the larger bigger contractor companies is probably still yet to come. I have spent time personally with some leadership of those public companies, and they're anticipating increased CapEx next year at a rate higher than depreciation.

So we have started to see that quote activity but they have not pulled the trigger. Of course they're just at the end of their budget process, but the private companies pulled the trigger quicker than the public companies when the bill was signed.

Q: Yes and what do you see, you mentioned asphalt plants, what are you seeing on the mobile equipment side, same trends?

Ben Brock - President & CEO
Same trends.

Q: Okay, how about you talked a little bit about the strong dollar being obviously an impairment to export, maybe the asphalt hot-mix or some of the mobile highway road building equipment. How much of a competition do you have from foreigners coming in and selling parts? Obviously time to market, service supply, repair parts, always customer service, that's real important, probably tougher to do that from Europe for a US domestic. But how much does the import compete against you guys?

Ben Brock - President & CEO
Not so much on the part side but on the major equipment side right now, it's a good bite on deals where they're involved. On the parts side we're finding we're gaining a little market share on supporting their equipment once they get here, if we lose the deal. Now we're seeing that not just in the US, we're seeing that in other countries.

Q: How price elastic, Ben, as you've said we have a pent-up demand, you guys expect a little lull, it's been pretty steady, how much price discipline is in there?

Ben Brock - President & CEO
I've made the comment last call, I remember putting my thumb in my index finger together and just barely pulling them apart and looking through, and it's maybe just a little bit further away from the thumb but it's not much. And it's really because all of the people that we deal with are shrewd buyers, and it's rare that we're ever alone. All of our competitors are working like mad to get the deals, too. So I think our guys have really done a nice job given as competitive as every deal really is and we're doing a little bit better at that but it's not a lot.

Q: Okay, all right. And then on the pellet plant side, as you guys begin building that up as an ongoing business, what kind of ongoing parts repair might be service for that business?

Ben Brock - President & CEO
It will be similar to the asphalt plants as far as the percentage. So I don't see it necessarily moving our needle on a percentage basis of part sales annually. But the more we can get out there it'll grow the volume. And so the top line hopefully keeps moving with it as we sell more pellet plants, too, but I see the parts businesses being fairly similar.

Q: Ben, on the part side as you have the pent-up demand, new equipment is obviously out in the field, specifically on the mobile highway side, do you see part sales maybe plateauing for a while as you're not grinding through used equipment? Or because there's a bigger infield installation of just sheer numbers do you see parts going along with it?

Ben Brock - President & CEO
I feel like we can still increase our part sales but partially what you're saying is true because when new equipment's out there it just takes less parts. But the other thing that we can work toward is support and competitor's equipment that they don't do as good a job on parts in the field.

And so that's and service sales, too, which would show up in parts. I still think even though to your point the newer equipment will take less parts, I think there's still an opportunity in service and support of other brand's parts. And because it's just hard to get people and we think that there's an opportunity in service sales as well that'll help our part side. It's probably better margin to be had in service.

Q: Okay. And then you guys mentioned the new products. Anything specifically that you're willing to comment on for ConExpo 2017?

Ben Brock - President & CEO
Very excited about ConExpo, excited about the number of new products that we're going to have on the floor. I think for competitive reasons if we can get asked that in the February call, I'd be happy to say but I think they've got long enough to react. I can say this, we will have more new products on the floor at this ConExpo than we had three years ago.

Q: Okay. And then just one final one, you talked a little bit about kind of capacity utilization I think at the asphalt hot-mix, and some of the mobile. What would be obviously the worst areas, what might be your toughest? I'm sure it's in mining in that or energy. What might be the lowest level capacity utilization you might have?

Ben Brock - President & CEO
Our GEFCO facility in Enid, Oklahoma is our number one challenge. And their utilization, Rick Dorris, our COO was here, is very low. It's almost embarrassingly low, so that's why we're moving brooms, street broom production there from Roadtec that could free up room for more mills and pavers to be built. It's our overload shops that we're trying—asking everybody do not outsource, let's in-source if you need capacity. So we're just trying everything we can to get man hours through there.

Good news is Jaco van de Merwe, whom I mentioned in the comments, our new group president of energy, came from Atlas Copco. His last assignment with him was in the drilling business in Texas. Although he's worked all over the world he's a native of South Africa. But he has a good vision and visibility into that market, and the products, and I think he's going to help them. It won't be an immediate effect but I think six to ten months from now I think we can be a much better position in Enid, Oklahoma.

Q: All right guys, congratulations, great quarter.

Operator
We've reached the end of our question and answer session. I would like to turn the floor back to management for any closing comments.

Steve Anderson - VP, Administration & Director, IR

Thank you, Brenda. We appreciate your participation on this third quarter conference call and thank you for your interest in Astec. As today's news release indicates the conference call has been recorded. A replay of this conference call will be available through November 8, 2016. And our archive webcast will be available for 90 days.

A transcript will be available under the Investor Relations section of the Astec website within the next seven days. All of that information is contained in the news release that was sent out earlier today. This concludes our call, and again, thank you and have a good week.