

## **Transcript of Astec Industries Third Quarter 2017 Earnings Call October 24, 2017**

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### **Participants**

Stephen C. Anderson - VP, Director of IR and CS  
David C. Silvius - VP, CFO and Treasurer  
Benjamin G. Brock - President and CEO

### **Analysts**

Joe Grabowski - Robert W. Baird  
Mike Shlisky - Seaport Global  
Stanley Elliott - Stifel  
Nicholas Coppola - Thompson Research  
Jon Fisher - Dougherty & Company  
Brian Sponheimer - Gabelli & Company  
Brian Rafn - Morgan Dempsey Capital Management  
Morris Ajzenman - Griffin Securities

### **Presentation**

#### **Operator**

Greetings, and welcome to Astec Industries' Third Quarter 2017 Earnings Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. As a reminder, this conference is being recorded.

I would like to turn the conference over to Steve Anderson.

#### **Stephen C. Anderson - VP, Director of IR and CS**

Thank you, Sherry. Good morning and welcome to the Astec Industries' conference call for the third quarter that ended September 30, 2017. Sherry mentioned, my name is Steve Anderson, and I'm the Vice President of Administration and Director of Investor Relations for the company. Also on today's call are Benjamin G. Brock, our President and Chief Executive Officer; Richard Dorris, Executive Vice President and Chief Operating Officer; and David Silvius, 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 as well as give some outlook going forward.

Before we begin, I'll 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. Factors that could influence our result are highlighted in today's financial new release, and others are contained in our annual report and our filings with SEC. As usual, we ask that you familiarize yourself with those factors.

So at this point, I'll turn the call over to David to summarize our financial results for the third quarter.

**David C. Silvius - VP, CFO and Treasurer**

Thanks, Steve. Thanks to each of you for joining us this morning. Our net sales for the quarter were \$252.1 million compared to \$247.8 million in Q3 of 2016. That is a 1.7% increase or \$4.3 million increase. Recall that on October 2, we announced that we would incur a charge related to new additional investment in the two wood pellet plants that we have delivered to Georgia and Arkansas. This charge resulted in an impact on EPS for the quarter and year-to-date of \$0.59 per share, and I'll discuss that a little later. But throughout my comments I will refer to this charge as the impact of new pellet investment.

For comparative purposes, I will also be discussing the impact of all pellet plant activity during the periods under discussion. The new pellet investment is a component of that all or total pellet activity in Q3 of 2017. So without the impact of that new pellet charge for the quarter, net sales were \$266.3 million for Q3 of 2017. That charge impacted sales because we are on a percentage of completion basis on the Arkansas pellet plant.

Without the impact of all pellet plant activity during the quarter, which includes the charge I mentioned, net sales were \$265.5 million for Q3 of 2017 and \$228.6 million for Q3 of 2016. That's an increase of \$36.9 million or 16.1% increase in the core business.

International sales were \$55.6 million this quarter compared to \$47.9 million in Q3 2016, a 16% increase or \$7.7 million increase. International sales represented 22% of sales in this quarter compared to 19.3% in the same quarter last year. The increase in international sales for Q3 of 2017 compared to the same quarter last year, occurred primarily in Canada, Brazil, the Middle East and Asia. Those increases were offset by decreases in Mexico, and Central America outside of Brazil, in Europe and the West Indies. For the quarter international sales increased in each of our groups.

Domestic sales were \$196.5 million in this quarter compared to \$199.9 million in Q3 2016, a decrease of 1.7% or \$3.4 million decrease. Without the impact of the charge for the new pellet investment, domestic sales were \$210.7 million for Q3 of 2017. And without the impact of all pellet plant activity during this quarter and the same quarter last year, domestic sales were \$209.9 million this year compared to Q3 2016 domestic sales of \$180.8 million. That's an increase of \$29.1 million or a 16.1% increase in domestic sales for the core business. For the quarter domestic sales increased in the Ag and Mining Group and decreased in the Infrastructure Group and the Energy Group.

Part sales were \$64.3 million this quarter compared to \$63.1 million in Q3 of 2016, a \$1.2 million or 1.9% increase. Part sales for each of the Q3 2017 and Q3 2016 periods represented 25.5% of total sales. For the quarter, part sales increased in the Ag and Mining Group and decreased in the Infrastructure and Energy Groups.

Foreign exchange translation had a positive impact on sales for the quarter of \$1 million; that is if rates this year were equal to last year's rates, sales would have been \$1 million lower this year.

Net sales for the year were \$872.4 million compared to \$820.9 million for the same period last year. That's an increase of 6.3% or \$51.5 million increase. Without the impact of the previously announced new pellet plant investments, net sales were \$886.6 million for the first nine months of 2017. Again, sales were impacted by that new pellet plant charge because we are on a percentage of completion basis of accounting for the Arkansas pellet plant. Without the impact of all pellet plant activity for the first nine months this year and last year, net sales were \$870 million this year compared to \$756.3 million last year, an increase of \$113.7 million or 15% increase in the core business.

International sales were \$185.5 million compared to \$144.6 million for the year-to-date period last year, a 28.3% or \$40.9 million increase. Those increases occurred primarily in Canada, Russia, Australia, Brazil and in Asia. These were offset by decreases in South America outside of Brazil, in Japan and in Central America.

International sales represented 21.3% of sales for the first nine months of 2017 compared to 17.6% of total sales for the first nine months of 2016. For the year, our international sales increased in each of our groups.

Domestic sales were \$686.9 million for the first nine months of this year compared to \$676.3 million for the same period of last year, a 1.6% increase or \$10.6 million increase. Again without the impact of new pellet investment, domestic sales were \$701.1 million for the year-to-date period in 2017, and without the impact of all pellet plant activity during the first nine months of this year and last year, domestic sales were \$684.5 million this year compared to \$611.7 million last year. That's an increase of \$72.8 million or 11.9% increase. Year-to-date, domestic sales were 78.7% of total sales this year compared to 82.4% last year.

Part sales for the year were \$214.1 million compared to \$201 million last year for an increase of 6.5% or \$13.1 million. Part sales were 24.5% of total sales for both the first nine months of this year and last year. Again, foreign exchange translation had a positive impact on sales for the year-to-date period of \$1.4 million; that is if rates this year were equal to rates last year sales would have been \$1.4 million lower.

Gross profit for the quarter was \$39.1 million compared to \$55.4 million in Q3 of 2016, a decrease of 29.4% or \$16.3 million decrease. The gross profit percentage then was 15.5% for the quarter compared to 22.4% for Q3 of 2016. Without the impact of the new pellet plant charges, the gross profit percentage would have been 22.6%, and without the impact of all pellet plant activity during this quarter and the same quarter last year, the gross profit percentage would have been 23.3% for Q3 of 2017 and 21.1% for Q3 of 2016. The absorption variance for Q3 of 2017 was \$200,000 under-absorbed compared to a \$6 million under-absorption variance for Q3 of 2016. That makes a positive change in the absorption variance of \$5.8 million.

On a year-to-date basis, gross profit was \$180.4 million compared to \$200.8 million for the first nine months of last year, a decrease of 10.2% or \$20.4 million decrease. Gross profit percentage then is 20.7% compared to 24.5% for the first nine months last year. And without the impact again of the new pellet investment on the year-to-date period, gross profit would have been 22.7%, and without the impact of all pellet plant activity during the first nine months of this year and last year, the gross profit percentage is 23.9% this year compared to 23.5% for the first nine months of 2016. The absorption variance for the first nine months this year is \$2.5 million over-absorbed compared to \$7.5 million under absorbed in 2016, a \$10 million positive change in the absorption variance.

SGA&E for the quarter was \$45.5 million or 18% of sales compared to \$44 million or 17.7% of sales in Q3 of 2016, \$1.5 million increase, or 30 basis points increase, and the drivers of that \$1.5 million are additional research and development cost or expenses of about \$900,000 in additional health insurance over Q3 last year of about \$600,000.

For the year, SGA&E was \$142.8 million or 16.4% of sales, compared to \$132.7 million or 16.2% of sales last year. That's a \$10.1 million increase or an increase of 20 basis points as a percentage of sales. The year-over-year increases occurred in ConExpo. Recall that we had ConExpo earlier this year. It was about \$4.6 million. We did not have that in 2016 and additional payroll and related cost and benefits of about \$5.6 million in the current year over the first nine months of last year.

Operating income or loss was \$6.4 million of loss in Q3 of 2017, compared to \$11.4 million of earnings in Q3 of 2016. That's a decrease of 156% or \$17.8 million decrease in operating income. Without the impact of the new charges for pellet plant investment during the quarter, operating income was \$14.6 million, and without all pellet plant activity in the current quarter and in the same quarter last year, operating income was \$16.3 million for Q3 of 2017, compared to \$4.3 million for Q3 of 2016. That's a \$12 million increase or 281% increase in operating income in the core business for the quarter.

On a year-to-date basis, \$37.5 million was our operating income, compared to \$68.1 million for the year-to-date period in 2016, a 44.9% or \$30.6 million decrease. Without the impact of new pellet plant investment during the year, operating income was \$58.6 million, and without all pellet plant activity during this year and last year, operating income was \$64.6 million for the first nine months of 2017, compared to \$45.3 million for the first nine months of 2016, an increase of \$19.3 million or 42.8% increase in operating income of the core business.

The effective tax rate is a little odd this quarter. It's 50.7% compared to 41.5% last year, and it's 31.1% on a year-to-date basis, compared to 37.6% on a year-to-date basis last year. And the drivers for the quarter and the year are the same, except that we had a loss during the quarter, and we have earnings for the year-to-date. So, the drivers for the high tax return in the quarter and the low tax rate were a combination of the pre-tax loss in the quarter that we incurred along with increased research and development credits in 2017 as opposed to 2016, benefits from changes in Tennessee tax law that reduced our tax burden in the state and a favorable adjustment related to our federal income tax filing for 2016, which we recently filed.

Net income attributable to controlling interest, so we had a net loss for the quarter of \$2.7 million, compared to \$6.8 million of income in Q3 of 2016, a decrease of 139.7% or \$9.5 million decrease in net income. Earnings per share for the quarter was a \$0.12 loss per share, compared to \$0.30 earnings for Q3 of 2016, a 140% decrease or \$0.42 per share decrease in EPS for the quarter. Without the impact of the charge for new pellet plant investment during the quarter, net income was \$11 million, or \$0.47 per diluted share. This means that the negative impact of the new pellet plant investment on the quarter and year-to-date was \$0.59 per diluted share, \$0.01 above the range we estimated in our October 2 press release. That's due to the estimate that we used for our September actual cost to be incurred.

So, as we built out that \$0.54 to \$0.58 per share estimate we had to estimate September cost to actually be incurred because we're on percentage of completion at the one plant in Arkansas. And we had to estimate the tax impact on the charges for both Georgia and Arkansas. And so those estimates came in a little different when the actual numbers came rolling in, and so we were off by \$0.01 off of that range.

Without the impact of all pellet plant activity during the quarter net income was \$12.1 million or \$0.52 per share for Q3 of 2017 and \$2.4 million or \$0.10 per share for Q3 of 2016 ex-pellets in both periods. That's an increase of \$9.7 million or over 400% increase in earnings ex-pellets. So the core business earnings per share increased \$0.42 per diluted share quarter-over-quarter.

Year-to-date net income was \$26.9 million compared to \$42.8 million for the year-to-date 2016 period, a decrease of 37.1% or \$15.9 million decrease. Earnings per share were \$1.16 for the year-to-date period compared to \$1.85 for the year-to-date period in 2016, so a decrease of 37.3% or \$0.69 per share. Again, the new pellet investment during the year-to-date period had an impact on the year-to-date period of \$0.59 per share. But without that new charge net income would have been for the first nine months \$40.5 million or \$1.75 per diluted share.

Without the impact of all pellet plant activity during the first nine months this year and last, net income was \$44.4 million or \$1.92 for year-to-date 2017 and \$28.3 million or \$1.22 for year-to-date 2016, an increase of \$16.1 million or 56.8% increase. So the core business earnings per share increased \$0.69 per diluted share for the year-to-date 2017 versus the year-to-date 2016.

EBITDA during the quarter was \$400,000 compared to \$18.1 million for Q3 of 2016, a decrease of 97.8% or \$17.7 million decrease in EBITDA. Without new pellet plant charges for the quarter EBITDA would have been \$21.4 million. And without the impact of all pellet plant activity in the quarters this year and last, EBITDA for this year's quarter would have been \$23.1 million compared to \$11 million in Q3 of 2016, a \$12.1 million increase or 110% increase.

EBITDA year-to-date was \$57.7 million compared to \$87 million for the year-to-date period last year, a 33.7% or a \$29.3 million decrease in EBITDA year-over-year. Without the impact of new pellet investment during the first nine months of 2017, EBITDA was \$78.7 million. And without the impact of all pellets this year and last year, EBITDA was \$84.8 million for 2017 and \$64.2 million for 2016, an increase of \$20.6 million or 32.1% increase in EBITDA from the core business.

Total backlog was \$385.5 million at 9/30 of this year compared to \$389.3 million at the same date last year, a \$3.8 million or 1% decrease in total backlog. International backlog at 9/30 of this year was \$76 million compared to \$63.7 million at the same date last year, an increase of \$12.3 million or 19.3%. Domestic backlog at 9/30 of this year was \$309.5 million compared to \$325.6 million at 9/30 of 2016, a decrease of \$16.1 million or a 4.9% decrease in domestic backlog. Excluding pellet plant backlogs, the 9/30/2017 backlog increased \$61.1 million or 25% compared to the September 30, 2016 backlog.

Moving to the balance sheet, our balance sheet continues to be very strong. We have receivables of \$109.7 million compared to \$111.8 million at this date last year. Days outstanding were 38.9 at September 30, compared to 40.9 at September 30 of 2016. And our inventory is \$399.3 million this year compared to \$399.7 million, or a slight decrease year-over-year, but our turns are at 2.5 turns this year compared to 2 turns last year.

We owe nothing on our \$100 million domestic credit facility, and we have at 9/30/17 \$68 million in cash and investments. Letters of credit outstanding are \$8.6 million at September 30, yielding a borrowing availability of \$91.4 million on our credit line. In Brazil, we currently have about \$5 million of debt used to finance that company's building fixtures and inventory.

Capex for the quarter was \$2.9 million, and for the year capex was \$14.4 million. For 2017 we're forecasting capex to be approximately \$22 million. Depreciation for the quarter was \$5.3 million and \$15.9 million for the year. For 2017 full year we're forecasting depreciation to be around \$22 million.

So that concludes my prepared remarks on the financial details. I'll turn it back over to Steve Anderson.

**Stephen C. Anderson - VP, Director of IR and CS**

Thank you, David. Ben will provide comments regarding the third quarter of this year's operations along with the outlook for Q4, 2017 and full year 2018. Ben?

**Benjamin G. Brock - President and CEO**

Thank you, Steve, and thank you, everyone, for joining us on our call today. As we commented in earnings release this morning, our wood pellet plant investments that we previously announced on October 2nd significantly impacted our earnings for the quarter. With the exception of the wood pellet plant investment impact we were pleased with our results for the third quarter, and we were pleased that ex-pellets we were able to grow sales and backlog while also shipping new products during the quarter.

I'll briefly cover a few of our actual financial results as usual; however, I'll also be referencing our ex-pellet financial reports for some core and future business perspective, although David has done a very nice job of trying to give a full picture of where we stand on those points.

Our third quarter sales were \$252.1 million versus \$247.8 million for an increase of 1.7%. Our third quarter sales ex-pellets were \$265.5 million, which is an increase of 16.1%. Our earnings per share for the quarter were a negative \$0.12 per share versus a positive \$0.30 per share in the third quarter of 2016. That's a decrease of 140%. Our earnings per share on new ex-pellets was \$0.47 a share positive versus \$0.30 a share positive for an increase of 57%. Earnings per share were mainly impacted by the wood pellet plant investment that we announced.



Infrastructure Group gross margin was 1.8% versus 22.8% last year. Ex-pellets Infrastructure Group gross margin was 21.9% versus 22.8% last year.

The Aggregate and Mining Group gross margin was 24% versus 24.4% last year. They had no pellet effect in their gross margin. They had new products that went out during the quarter with gross margin slightly below expectations, but very much in line with our projections.

The Energy Group was a bright spot with the gross margin of 24.9% versus 18%, again no pellet effect in the Energy Group. They maintain good industrial product shipments, which carries a little higher gross margins and improved their oil and gas and water well shipments out of the group.

Year-to-date consolidated gross margin was 20.7%, and year-to-date consolidated gross margin ex-pellets was 23.9% versus a gross margin of 23.5% ex-pellets last year. And as David mentioned, year-to-date EBITDA was \$57.68 million against a rolling 12-month EBITDA of 6.95% of sales versus 9.54% last year. Ex-pellets our year-to-date EBITDA is \$84.8 million, which gives us a year-to-date EBITDA of ex-pellet percentage of 9.7% versus 8.5% last year.

Our backlog at September 30th was \$385.5 million, down less than 1% versus last year. That's an improvement versus last quarter's down 5% versus last year. Excluding pellet plants and including historical Power Flame backlog levels, our backlog is up 24.8% versus last year, nearly keeping pace with last quarter's, up 27% versus last year.

Our Infrastructure Group backlog was down 13.2%, an improvement from being down 20.4% at the end of the second quarter. Again, the infrastructure backlog was down mainly due to not having a large pellet plant on order. The group continued good order intake on non-pellet plant products during the quarter, mainly as a result of the Federal Highway Bill in the U.S., state and local funding mechanisms to improve road and bridge investments and improved international activity.

Excluding pellet plant backlog, our infrastructure backlog was up 18.7%, an improvement from being up 18.6% versus last year at the end of the second quarter. Order activity has remained slightly above normal in the group since October 1st.

Our Aggregate and Mining Group backlog increased 21.5%, mainly as a result of that Federal Highway Bill, state and local funding mechanisms and continued good execution securing international sales. Our Energy Group backlog was up 51.2% as we continue to experience good order intake in the group for products targeted at the construction industry along with increased order activity for water, oil and gas drilling products.

Our total company domestic backlog was down 4.9% year-over-year, and our international backlog was up 19.3%. Our order backlog in domestic was again primarily not to have a large pellet plant on order. Domestic backlog excluding pellet plants was up 26.8%, essentially flat from being up 27% versus last year at the end of the second quarter. But indicative of a good market for our core products as we kept pace on orders during the third quarter, which can be a slower order quarter as our customers work in the summer months.

Regarding our increased international backlog, we continue to experience slight improvement in quoting in international and our sales groups have done a nice job of getting orders on much of what we are quoting. Our increased backlog international is once again a direct result of the pent-up demand from customers and our team executing where we could for those orders.

We mentioned on our last call that our Astec do Brazil, the subsidiary, experienced a very, very slight increase in quoting activity in Brazil, and we are pleased to report that the subsidiary still has a small backlog. However we believe that the economic and political environment remains a challenge to us for the rest of this year and likely most of next year in Brazil. While we are keeping a long view with regards to international, we do see challenging currency conditions remaining in place.

Changing subjects to wood pellet plants, David has covered the accounting with regard to the pellet plant investments and done a nice job again on that. On October 2nd, we did announce that we had initiated the significant design upgrades to our customers' plants in Georgia and Arkansas to meet full product for wood pellets. We identified significant design issues that are at the Georgia and Arkansas pellet plant sites driven by the need for both facilities to achieve full product rates. Upon learning on those design flaws which were different in each plant, we identified a clear path at both sites to achieve the necessary results for our customers in the near-term. As many of you know, one of our core values is delivering superior service to our customers, and we have a high level of confidence that we have identified the issues and are underway in making the necessary upgrades to achieve full production in Georgia and Arkansas.

Also on October 2nd, we announced that we had completed the analysis of the necessary all-inclusive investment needed to deliver on our commitments to our customers, which we expected to negatively impact our third quarter earnings by \$0.54 to \$0.58 per share. As David explained, the impact ended up at \$0.59 per share.

We were very disappointed to be announcing that at investment on October 2<sup>nd</sup>, but we wanted to make sure we provide a swift disclosure of the adverse impact on our overall financial results for our third quarter as well as make the necessary improvements to the plants to maintain a high level product for our customers.

As a reminder, our financial investment in the pellet plant business started in December of 2010 when we opened a work order that design, build, direct and operationally run a five-ton per hour prototype pellet plant on our property at our Astec, Inc. subsidiary. The prototype plant started up in September of 2011 and ran through May of 2012 and gave us the confidence to pursue the largest order in our history at the time with Hazlehurst Wood Pellets in Georgia. The last segment of that order was received on January 30, 2014.

Due to market conditions, the plant was not pushed to run at full capacity and it was also run with natural gas as a main fuel source. Market conditions have since improved, and as a result the plant now needs to run at full capacity with wood as a fuel source. As we've looked to ramp up production rates the series of design flaws were uncovered, and we're working diligently to correct them now.

Our experience at the Georgia site early on gave us the confidence to pursue the largest single order in our history with Highland Pellets in Arkansas. The last segment of that order was received in March of 2016. This plant also has been running at low production rates, and as we ramped up production, we found design flaws as well that are different than those we are experiencing in Georgia.

As another reminder, I want to reiterate as we mentioned on our call on October 2nd, the design flaws we uncovered in Georgia and Arkansas were identified in the 45 days before the October announcement. In addition, to avoid any confusion on Arkansas, these upgrades are unrelated to the construction related cost issue we experienced during the second quarter, which we believe is behind us.

While the design issues are not identical at both sites, they each require full attention and effort to get them into full production. We are confident in our ability to do so for our customers, and the investment we have announced is the amount that we believe will cover the entire cost associated with completing our commitments to our customers with regards to production rates. I am pleased to report that we are on schedule with regards to completing our commitments at this time.

Despite the announcement on October 2nd, we are very confident in the near-term and long-term outlook for pellet plants, and our success at these sites will put us in a strong leadership position for orders as we move ahead. Including the announced charge on October 2nd, we will have invested approximately \$31 million over seven years to get into a \$100 million per year business. We believe that the investment is a good one for our company.

In the last seven years, we have remained profitable, acquired six companies, added additional capacity at several subsidiaries, had a most successful ConExpo show with 33 new products and grown our cash on hand, all while remaining debt free. In addition, our balance sheet remains strong, our core infrastructure business is very good, our energy business has attractive tailwinds, and our international business has continued to be ahead of last year.

With regards to the Hazlehurst Georgia plant that we have discussed on several calls, as a reminder, it was a new product that we chose to finance, and as a result, we've recognized revenue on these plants as we're paid. This will have an effect on our cash and inventory until it's paid in full. The order for all three lines is for \$60 million, and we expect final payment in December of 2018. As a reminder, the interest rate on it was 6%. With regards to Hazlehurst, please keep in mind that we are carrying it on our books at breakeven so its effect to us is on our inventory and cash.

Updating our current pellet plant quote activity, we will not take an order for another pellet plant until we have passed the production test at the plants in Georgia and Arkansas. We expect to complete these tests no later than April 15, 2018. We do have active pellet plant quotes in process. Going forward we will only supply pellet plants as equipment suppliers. We will not act as the EPC, which means that we will not supply site or civil work, nor will we act as a general contractor for the whole project. The customers we are quoting at this stage understand our position and are okay with our position.

Changing subjects to the Energy Group, we were pleased with the increase in gross margin in this group, and we are encouraged by the third quarter in a row of increased backlog for the group. Sales of wood chippers and grinders remained consistent during the quarter. Our concrete plants are built in the Energy Group, and quoting activity is very good for our plants. We are happy to report that we have secured another order for our CEI style ready-mix concrete plant. We were pleased to increase backlog at our GEFCO facility as well.

We remain optimistic on our outlook in the Energy Group in the long-term. As a reminder, our new product development continues in all groups; however, at a slower pace than we had going into ConExpo. We are focused on selling the new products from the show and increasing gross margin.

Looking ahead to the fourth quarter of 2017, while we are encouraged by our historically good backlog, we are cautious for the fourth quarter due to product mix and contracted delivery dates. Given these two items and the normal Thanksgiving and Christmas Holiday schedules we believe that our fourth quarter 2017 earnings per share will be slightly below our new ex-pellet EPS as David mentioned, which was \$0.47 per share.

We believe that our fourth quarter revenue will allow us to be slightly ahead for 2017 versus 2016 total revenue. We are pleased with our domestic infrastructure product sales activity, our continued oil, gas and water product sales activity and our international sales team success given the challenging environment they face with regards to the strong U.S. dollar. As we look ahead to 2018, we see revenue growth of 5% to 10% with an improved net income versus the net income as David mentioned with the new ex-pellet earning side.



With the exception of the wood pellet plant investment during the quarter, our Infrastructure Group is performing well and has a good backlog. We remain optimistic on our outlook for our Aggregate Mining Group and despite the good backlog in the Energy Group we remain slightly cautious on the near-term outlook in the Energy Group.

From our last earnings release to now, orders have been good in the Infrastructure Group and in Aggregate Mining Group mainly due to the highway bill and international sales. Energy Group orders are improved for products targeted at the water and oil and gas industries with slight increased quoting activity. Orders in the Energy Group are good for products targeted at infrastructure customers. Aggregate Mining Group orders remain soft for products targeted at the mining industry; however, we continue to see slight signs of potential improvement in the mining industry for our products.

Bright sponsor activity are hot mix asphalt equipment sales, both asphalt plants and mobile equipment, asphalt rubber blending system quoting activity, water well drilling and oil industry related equipment sales, wood grinder and chipper sales, concrete plant sales, aggregate crushing and screening equipment, quoting and sales activity and international quote activity despite the strong dollar.

Year-to-date part sales were up 6.5% versus last year and were 24.5% of total sales. We remain committed to improving our part sales volume in the long-term along with working to continue to increase competitive part sales. The majority of our customers in the United States are experiencing a stable private market, and we're focused on selling existing and new products.

Turning now to our announcement of our acquisition of RexCon, LLC on October 2nd, we are very pleased to welcome RexCon to the Astec Industries family of companies. RexCon is a successful, profitable company with reputation for innovative technology and dependable quality products, and we are a match culturally and in our approach to business. RexCon joining our family of companies reflects our stated strategy to continue to focus growth both organically and through acquisitions of strong companies that serve in infrastructure, aggregate mining and energy industries. RexCon will continue to operate as RexCon, Incorporated in Burlington, Wisconsin and will join our Energy Group.

We thank Jake Jacobs and Mike Redmond, the owners of RexCon, for their collaborative efforts in making this transaction happen, and we are pleased that they will continue to run and grow RexCon as a part of Astec Industries. For those of you that are not familiar with RexCon, RexCon engineers, sells, manufactures, services and provides aftermarket parts for concrete production facilities which are also known as concrete plants. They build stationary re-locatable and portable plants as well as components for those plants. RexCon is the number two position with regards to concrete plant market share in the United States.

The concrete plant market in the United States is a fragmented market and we believe that we have the real opportunity to be number one in concrete plants with RexCon and CEI in the very near-term. As a reminder, the purchase price was \$26 million, which was paid after the end of the quarter. So when you look at the cash and investments of \$68 million, we spent \$26 million early in the fourth quarter. This represents an acquisition in the range of six to seven times EBITDA. Acquisitions remain a part of our growth strategy along with organic growth. To that end, we continue to work on potential additions to our Astec family.

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 back over to Steve Anderson.

**Stephen C. Anderson - VP, Director of IR and CS**

Thank you, Ben. Sherry, I believe we're ready for any questions there may be, so if you would poll the callers, we'd be glad to take those as they come.

**Operator**

Thank you. At this time, we'll be conducting a question-and-answer session. [Operator instructions]. Our first question is from Mig Dobre with Robert W. Baird. Please state your question.

**Q:** Hey, good morning guys. This is Joe Grabowski on for Mig this morning.

**David C. Silvius - VP, CFO and Treasurer**

Good morning, Joe.

**Q:** So, thanks for all the additional color on the statistics ex-wood pellet plants. So I think I heard that sales in the third quarter were up 16% ex-wood pellet plants and year-to-date up 15% ex-wood pellet plants. What would the guidance of slight sales increase for the year implied for fourth quarter sales ex-wood pellet plants? So I know you have your toughest wood pellet plant comparison fourth quarter 2016.

**Benjamin G. Brock - President and CEO**

Hi, Joe. This is Ben. Last year we ended at I think \$1.147 billion, and I would say in that range of 1% to 2% over that for total sales for the year.

**Q:** Right. But what does that imply for the fourth quarter, ex-wood pellet plants?

**Benjamin G. Brock - President and CEO**

I don't know if we run that number that way.

**Q:** Okay.

**Stephen C. Anderson - VP, Director of IR and CS**

Yes, we can get back to you with the wood pellet sales in the fourth quarter. We've have already disclosed that last year. So the 1.2, we should be able to get back into that for the revenues, Joe.

**Q:** Okay, no, that's fair. And then do you have a feel for what the guidance of EPS slightly below Q3 implies for gross margins in the fourth quarter?

**David C. Silvius - VP, CFO and Treasurer**

I think the gross margins would be reflective of the Q3 performance. If we're looking at EPS in the Q3 range, then I would think that gross margins would be reflective of Q3 gross margins. You are going to potentially have some pellet revenues in Q4 depending on the cost that we incur through a percentage of completion at the one plant, and those would come in at significantly lower gross margins, like we said on our October 2 phone call. Those would be in the 5% range. But those would be a small dollar amount of sales. And so I think Q3 ex-pellets gross margins as we described would be a good place to start for Q4 gross margins.

**Q:** Great, okay, got it. And then corporate expenses, if you've mentioned this on the call and I missed it, I apologize. But corporate expenses were unusually low in the quarter. What was going on there?

**David C. Silvius - VP, CFO and Treasurer**

Well, we've actually started to curtail a little bit of R&D. We get geared up for R&D for ConExpo, and now we have a lot of those new products going through the shops. And so R&D is going to be more normalized as we enter 2018, we believe. That's one area. We didn't have some of the more significant health insurance costs. You know how those things bounce around and you hate even talk about them, but they are real, and when you have some certain experience with those healthcare costs, those things bounce around.

And obviously as we have profit share, if you will, and when your profit is not high, then the profit share is not high either. So the accruals for those payroll and related type things that are driven by performance are lower this year than they were last year.

**Q:** Got it. And then just couple more quick questions on the—I think Ben mentioned from 2018 guidance in his remarks sales up 5% to 10% in 2018. I assume that does not assume an additional wood pellet plant, any additional wood pellet plant revenues in 2018.

**Benjamin G. Brock - President and CEO**

Yes, Joe, this is Ben. It really doesn't. We have the opportunity depending on timing for some pellet business in the fourth quarter, but we're not going to bank on that. That's most likely more of a 2019 event for us.

**Q:** Great. And then last question on 2018 guidance. Improved net income in 2018, is that sort of ex all the wood pellet plant noise in 2017. If you kind of back that out, net income would still be higher in 2018?

**Benjamin G. Brock - President and CEO**

Yes.

**Q:** Great, okay. Thanks for taking my questions.

**Benjamin G. Brock - President and CEO**

Thank you.

**Operator**

Our next question is from Mike Shlisky with Seaport Global. Please state your question.

**Q:** Hey, good morning, guys.

**David C. Silvious - VP, CFO and Treasurer**

Good morning.

**Q:** I wanted to just quick follow-up on a few of Joe's questions first. I guess the first one was your outlook for slight increase for the year in sales. Asked a little bit different way, when you exclude the pellet plant business, can you tell us the range of growth that you're expecting for the year excluding all pellet plants?

**Benjamin G. Brock - President and CEO**

I guess we've got pellet plants in the number that—this is Ben, Mike. In our number and my saying up slightly for the year, that has everything in it. So we're saying for last year we had everything, we had pellets in last year and we are at the 1.147 range. We're saying we'd be up 1% to 2% with all pellets in. We have not run it without pellets in that way.

**Stephen C. Anderson - VP, Director of IR and CS**

We've given you the through third quarter wood pellets and also the projected or what's left about on wood pellets for fourth quarter. So you'll have enough to back into that.

**Q:** Okay. Well, how about this way, so through the first three quarters of the year, you mentioned that excluding pellet plants your sales were up about almost 12% in the first three quarters, I think. Are we in the similar range in the fourth quarter or is there some big decline that you expect to take place in the fourth quarter just broadly speaking?

**David C. Silvious - VP, CFO and Treasurer**

This is David. We were up 15% year-over-year ex-pellets, ex-all pellet activity. And for the fourth quarter, if you think about what we're saying that we're going to be similar EPS, similar gross margin we believe in the fourth quarter, then when you look at the sales, I mean, ex-pellets we're up 15% year-over-year, but with pellets we're up 1.7% through the nine months. I think you're going to find similar ratios in the fourth quarter.

**Q:** Okay. I'll sit down with the old calculator a little bit later, no problem. Also I want to ask another one of Joe's questions a different way about the incentive comp. In the third quarter, was there a big sort of positive on incentive comp? Because you had a large loss in the quarter. And so will you have to true it up next year if you go back to a more normalized profit environment, or will there be a large increase in your incentive comp expecting in 2018 assuming your sales were up by 10% next year?

**David C. Silvious - VP, CFO and Treasurer**

Yes, it typically moves with the pre-tax profit, with the return. We measure return on capital employed internally, and that's a big driver, EBITDA that sort of thing. So there is going to be an increase, and as a percentage of sales or the overall performance of the company, it's probably not going to be any larger. But it moves up and down with performance.

**Q:** Okay, I get that. Alright, secondly I just want to also ask quickly about some of the issues you're seeing in the fourth quarter on delivery schedules. Can I just get a little bit more color there? Is it because you're seeing some difficulties in finding trucks to do deliveries? There has been some disruptions in certain parts of the country because of the weather and also just a pretty solid environment for a lot of different pieces of machinery out there. Is it hard to find platform trucks to get things delivered these days? Is that part of the caution in the fourth quarter?

**Benjamin G. Brock - President and CEO**

No, Mike, we haven't really heard of any issues for us being able to transport equipment. For us it's more of the dates when people are ready to take on them and the contracted delivery dates. It's a little bit of the products that are going through is just the timing. We always have the holiday, so that's hard to kind of say that's a reason, but it's more of what we've picked up through our travel in all the divisions and looking at what we have to ship and the timing of everything. We're just not going to have a huge fourth quarter.

**Q:** Okay. And then I wanted to touch briefly on the infrastructure numbers as well. Other companies out there and I think also in mining, you have other companies there. Some of them had their calls today looking at growth of 20% this year in construction type equipment and 30% in mining, and I'm not getting the sense that you are quite seeing the same growth. I know there are different products. But even some of your comps in Europe are seeing mid-teens growth this year. Is there anything we should worry about here on market share or is it just simply delivery days that would make Astec sales not be in the ballpark of other major players in the industry right now?

**Benjamin G. Brock - President and CEO**

I think to be fair on ours, our mining has never been a huge piece of our business. Most of that for us is in South Africa with our Osborn Group and then Brazil which we have a struggle on that region for a lot of different reasons. But that's what we referenced in the comments that we're seeing a little bit of an uptick in quoting. We're starting to see that, but usually in our Aggregate and Mining Group most of that business is in the aggregate side, the quarry, the construction products aggregate side, and that part is up pretty well for us.

**Q:** Okay, I'll leave it there, guys. I appreciate it.

**Benjamin G. Brock - President and CEO**

Thank you.

**Operator**

Our next question is from Stanley Elliott with Stifel. Please proceed with your question.

**Q:** Hey, guys, good morning. Thank you for taking the question. Just in kind of with all the moving parts it would have been helpful to have a little bit of a table, I guess, just to kind of in the for what it's worth category, but can you guys talk about the pricing environment? What's happening out there in terms of the quoting activity and things like that in terms of where we are on pricing?

**Benjamin G. Brock - President and CEO**

Stanley, this is Ben. We have a little bit of pricing, I guess, pricing power. I think it gets hard with all of our customers always have two, three or four people in against us on deals, but we have been able to get a little bit more. I think you're seeing that a little bit in our ex-pellets margins year-to-date and we in our high side again on margins the last step cycle 25% to 26% gross margins. We really see an opportunity to be there in this second half of next year.

Steel is a big input cost for us. We've been doing a pretty good job of managing that. We're in pretty good shape into the first quarter at most of our places, but the steel guys are always talking about raise in prices. So we keep up a strong eye on that. We worked on our pricing in September and October already. So we feel like we are able to get a little bit more. I mean there is definitely demand there to do it.

**Q:** Perfect. And then could you just remind us with the investments that you have made, where are these plants now, the wood pellet plants running on a tons per year, tons per hour, any sort of metric that you can help us within that?

**Benjamin G. Brock - President and CEO**

There are two different plants, two different tons per hour and even the modular lines that we supply the plant in Georgia is three 15-ton-per-hour lines, so 45 tons an hour there. The plant in Arkansas is 20-ton-an-hour lines. There are four of those line, so 80 tons an hour there. We're running one line and they are selling pellets out of Hazlehurst. We're doing the corrections on all lines kind of as we are going to be able to run on wood.

And we are expecting to test that mid-November there and then at Highland in Arkansas, it's a little more involved frontend work with green hammer mills, cement plant work. They are running. They are running at low production rates; they're selling pellets out of that plant. But to ramp up and go to 20 tons an hour on all four lines at the same time and do the test there, it's a lot more involved, and that's the April drop dead date that we've mentioned in our comments.

So, we have been at full production on individual lines at both places, but we've done it on gas mainly at Hazlehurst. Wood is a requirement for a long-term contract, so we're working on the wood part of that as we talked about on our last call. We had run on wood until you run all three of them and start trying to push it up. That's where we hit our limits and found out issues as we went through time on bag houses down there. But different issues at Arkansas, but we have run one of the lines at 20 tons an hour. But consistently doing that on all lines, is our ultimate target. And so that kind of, and maybe more than you ever wanted, but that's kind of where we are. We know what to do, we just have to execute it.

**Q:** I appreciate that. And the last one for me, so with the drop dead date November, then kind of April in terms of guaranteeing the throughput. If the monies that were kind of spent in the quarter to upgrade and modify, if that doesn't solve the problem, then is Astec responsible for additional capital outlays to get those to meet the said throughput?

**Benjamin G. Brock - President and CEO**

In the unlikely event that we don't, we would be.

Q: Great, guys. Thank you.

**Benjamin G. Brock - President and CEO**

Thank you.

**Operator**

Our next question is from Nicholas Coppola with Thompson Research. Please state your question.

Q: Hi, good morning.

**Benjamin G. Brock - President and CEO**

Good morning.

Q: I just want to follow up on that last question. Do you have any sense for how much investment in the wood pellet plant and wood pellet plant upgrades should occur in Q4?

**Benjamin G. Brock - President and CEO**

That would be cash only because all of the charge is in the third quarter.

Q: Okay. So no impact to gross margin?

**David C. Silvius - VP, CFO and Treasurer**

No, there wouldn't be any impact to gross margin; the only impact to gross margin would be on percentage of completion if we were to catch up to where we had previously recognized sales. In other words, if we get back to 95% complete or whatever the number is, then we would recognize some sales. Those sales would come through at around a 5% gross margin. There are in the range of \$17 million of sales left to be recognized on the Highlands plant.

And as Ben said, there is nothing to be recognized on Hazlehurst until December of 2018 in Georgia. On the Highlands plant, it really depends on how much cost is incurred, and in the Q4 that will drive the amount of revenue to be recognized. If there is revenue recognized, which we think there will be, but we just don't know how much, it won't be any more than \$17 million, probably significantly less than that.

Q: Okay, I appreciate that. That's a great clarification. And then just on infrastructure end markets can you talk at all about areas of strength across the U.S. and maybe one particular area to drill on would be California. I am interested in kind of hearing if you are seeing folks invest in equipment ahead of the greater spending that we expect to see in that state.

**Benjamin G. Brock - President and CEO**

Yes, Nic, this is Ben. From an area standpoint it's pretty strong still coast-to-coast, and in California in particular we have some major asphalt plants being delivered. So we have already seen that activity. We have seen some activity on the mobile side. We have not traditionally been as strong out there with our Roadtec Group, but we have gone to a dealer model in that company, and that has turned out to be a very good move. We are seeing a little uptick in California, but a lot bigger uptick in the states touching California.



So, we're optimistic on how that will play out long-term. Our Carlson Group with the commercial style of pavers and the screed business are doing extremely well in that region and really across the country. But really proud of what they are doing with their new pavers in the screed business.

**Q:** Okay, that's great. And then, one last question on energy. Backlogs there up 50% year-over-year, quite strong. And I heard in your opening comments you called out construction water and oil and gas products doing well. I guess within that are there any standouts, any color you can add as to how I guess how you achieved that kind of growth?

**Benjamin G. Brock - President and CEO**

Well, the double pumpers that are built at our GEFCO facility, we've gotten some nice large orders in that and some larger international water drill rig units. As a description it looks like a monster truck, guys. But it's a drill rig in the Middle East to drill for water. We have a couple of orders on that, so that's been a bright spot.

And then we've gotten some food industry orders too in that group. That's not really construction related, but the Heatec division has gotten some nice industrial business in the back half here too, so that's been another good pick-up. And then at CEI, mentioned in the region, California is where that ready mix concrete plant is going.

It's good. I think it's been down long enough that we stay cautiously optimistic on the short-term and still really optimistic in the long-term, but it has an opportunity to stay pretty good through 2018.

**Q:** Alright. Well, thanks for taking my questions.

**Benjamin G. Brock - President and CEO**

Thank you.

**Operator**

Our next question is from Jon Fisher with Dougherty & Company. Please state your question.

**Q:** Good morning, everyone. Just the 2018 revenue growth outlook commentary of 5% to 10%, that includes RexCon and includes the fourth quarter wood pellet plant payment?

**Benjamin G. Brock - President and CEO**

Yes. Well, I say that not on the wood pellet plant. I think it could be a little bit more, Jon. It's a good question. And that 5% to 10%, I hate to be an "I" guy, but I frame that out, and that's a great question. That could be on top, but there is no earnings on that pellet plant. So that's probably in my mind why I didn't say that in the top-line. It's a breakeven event. So great question; thanks for asking that.

**Q:** Okay. Because the follow-through on that question was I was going to ask your opinion given the strong backlog growth that you've put up this year, kind of what your sentiment was on 5% to 10% revenue growth off of a year of consistent steady mid-teens to mid-20% backlog growth, I mean, if you thought that was good translation or not including RexCon and including the fourth quarter wood pellet plant payment.

**Benjamin G. Brock - President and CEO**

Jon, there is a little bit of hedge in the back of my mind. There are still two years left in the highway bill. We don't know what Congress is going to do on tax reform and infrastructure. And so it could be we see still a really pretty good year. We really think it's going to be a pretty good year, but is there going to be a slight summer doldrums that hasn't been there? That's the hedge.

Because to your point, we've seen the teens growth. That's where the reservation comes in. So when you start to say okay, what do we really think, the prudent thing to say is 5% to 10% in our business. Is there an opportunity? Sure. I mean we definitely would think there would be an opportunity, but when we're saying what we really think and we're going to hear about it again later next year, 5% to 10% would be the number.

**Q:** So from a business flow-through standpoint, double-digit backlog growth this year kind of flows through for the most part intra-year. The turn on that backlog growth is fairly quick within a quarter or two?

**Benjamin G. Brock - President and CEO**

Yes.

**Q:** Okay. Alright, that's good color there. And then just your comments on Brazil, since you went ahead and made some cautionary outlook comments on Brazil, just from a business impact standpoint, should we be concerned about just from a revenue impact or an earnings impact if Brazil is inordinately weak in 2018, any sort of negative ramifications financially that could have? I wouldn't think Brazil specifically would be that significant to your financials.

**Benjamin G. Brock - President and CEO**

No, Jon, it's not. We actually have it to where it breaks even and makes a little money right now in size. And we think that's adequate for next year. So we don't think there will be a significant effect there.

**Q:** Okay. And then just one last question on SG&A spend. Pretty comfortable with the current spend rate on SG&A given all the undulations in revenues, and when we look at the outlook for SG&A growth next year, would you expect that to be less than or in line with revenue growth?

**Benjamin G. Brock - President and CEO**

In line.

**Q:** Okay. Okay, thank you very much.

**Benjamin G. Brock - President and CEO**

Thank you.

**Operator**

Our next question is from Brian Sponheimer with Gabelli & Company. Please state your question.

**Q:** Hey, good morning, guys.

**Benjamin G. Brock - President and CEO**

Good morning.

**Q:** Just a quick one. The DNA of this company is that of a decentralized organization, and you've had to get I'm sure more involved on the wood pellet plants and you normally would have with the business. Has this experience in any way led you to consider maybe the breadth of the business's ability to have so many underlying operating segments?

**Benjamin G. Brock - President and CEO**

Brian, this is Ben. More of what we have come away is that we're unlikely to do very large projects like this, which is a big step out from our model of the big project work in managing those projects. That's the biggest takeaway.

From the collection of the companies we have and how they overlap with our customers in the field and the focus of Energy, Infrastructure and Mining, we're still very comfortable with that.

And we're very comfortable even with the pellet plants when we get to other sizes, this pain that we're going through, because we're going to have a great product that makes pellets. We're going to be really alone in the market as a solution for a plant that everybody knows will work coming out. And so I think the biggest takeaway for us is we're not big project managers, we're equipment suppliers and we need to stick to what we're good at. That's what we're good at.

And I think long-term the pellet plants are going to pay off. That October 2nd day was not a great day for us, nor were the 40 days leading up to that either. But I think long-term it's going to be okay, and I think we're very comfortable with our model once we get through the issues we've got at the pellet plants.

**Q:** Well, best of luck in getting through the speed bump, and good luck for a great fourth quarter.

**Benjamin G. Brock - President and CEO**

Thank you.

**Operator**

And our last question is from Brian Rafn with Morgan Dempsey Capital Management. Please state your question.

**Q:** Good morning, guys.

**Benjamin G. Brock - President and CEO**

Morning.

**Q:** Let me ask and you've talked about it a little, Ben, I guess a little different way, but if we look at your core infrastructure on the highway transit side, you look at billing your screeds, your asphalt, your hot mix plants, your pavers, what kind of a run rate do you see in the current cycle? I think it was almost ten years to get the FAST Act done in 2015. What do you see as runway out with the FAST Act and some of the state DOT budgets? And then as an adjunct to that, does the infrastructure talk with President Trump and then maybe an infrastructure bank, does that extend that at all or is that just a lot of political rhetoric?

**Benjamin G. Brock - President and CEO**

Brian, kind of the previous question on the 5% to 10% the highway bill has a few years left on it, and I think there's a couple to three years that could be very good still with that, that maybe some more traditional summer months where there is more work and that we see maybe more traditional summers but still higher than the low side when we had extension after extension after extension. So the environment is good for two to three years.

The thing about when you talk about Trump, I mean, being in and traveled about over 30 states this year and talked to a lot of owners, just talking to a lot of our customers, nobody likes how that guy is going about his business as president, but everybody agrees with what he wants to get done. But he can't send himself a bill to sign to clear the decks to do an infrastructure bill. So they have to get tax reform done or something done with healthcare to put the mechanism in place to be able to do an infrastructure bill, and then I think absolutely, the appetite is there in DC to get that done.

But we've got a House and a Senate that refuses to do their job. And so they've got it all, it's all road-blocked. I'm not trying to stump for politicians, but at the end of the day no president can send himself a bill to get something done. And so if that happens, I think there will be an infrastructure bill and I think it will extend this. I think it gets extended two to three years on top of what we already have.

I don't think that it will be \$1 trillion bill. I think it would be \$200 billion to \$400 billion, but that's a great number, because the current—and that will be mainly roads and bridges. And so the current highway bill is \$205 billion of roads and bridge work. So that would be very good for our industry. So we would definitely welcome it, but that environment up there, man, it's tough.

**Q:** Yes, chaotic. I get that. I appreciate the color. Looking across your different businesses, what might be your range of capacity utilization? Where is it tight and then where do you guys have capacity?

**Benjamin G. Brock - President and CEO**

It's tightest in the Infrastructure Group. We're probably running about 80% in the Infrastructure Group. Next tightest would be in the Aggregate Mining Group, 70% to 75% range, and then in the Energy Group still probably despite how well they've been doing in the 65% to 70% range, which would put us overall in probably a 70% to 75% utilization. We have lost a few deals on the asphalt plant side to delivery, but our market share is still as strong as ever. We don't like losing any deal on delivery. But all-in-all, we can't complain about our market share there. We think we're gaining market share in pavers, for sure.

**Q:** Okay, awesome. The RexCon deal in Burlington, you talked about mating that with CEI. How big is that market in concrete production plants? Is it primarily domestic? Is it global? Give me a sense as how big that is.

**Benjamin G. Brock - President and CEO**

Well, it's for us, RexCon has done international business, but their main business is U.S., Canada. And there are five main competitors in that space in our estimation, and we estimate it at a pretty evenly split market and maybe \$150 million to \$175 million. If CEI could have a good year and RexCon have a little bit better year next year and with the crossover of our customers, probably 70% of our customers on the asphalt plant side have concrete plants.

We feel like we should be with a target goal of being number one in concrete plants by the end of next year. And so I would say then with that, we have to execute. But the opportunity is there.

**Q:** Okay. Being up in Wisconsin, we got a ton of rain through the 4th of July, almost 40 inches of rain. Burlington was flooded. Do these guys have any problem with their plant, water damage or anything?

**Benjamin G. Brock - President and CEO**

Thankfully no. They're in a good spot where they are. It's a great facility.

**Q:** Okay. And then just on the wood pellet, you guys, a little bit of a pause, stepping aside. You talked about some of the big project stuff. Does that at all translate to customer cancellations, or perhaps as you guys pause a bit to reengineer, do you have other competitive entries coming in, or how does that look for 2018?

**Benjamin G. Brock - President and CEO**

We're not aware of anybody working to be a complete pellet plant supplier like we are. And if we miss a deal, we miss a deal. We don't want to take a deal until we're through these plants, and we think it's better to be finished and then move on for the next one. But we do have customers that know our timing and know what we're doing. So we feel like we have an opportunity for a large order on the other side of what we're doing.

**Q:** Okay. And then just on commodity raw materials, you talked a little bit about the steel side. Anything else—paint, oils, resins, anything from a feedstock standpoint?

**Benjamin G. Brock - President and CEO**

Generally, I think we've been able to hold our own on that. There is pretty good competition on those things. And really steel is the one we're watching the hardest right now.

**Q:** Okay, thanks, guys. Appreciate it.

**Benjamin G. Brock - President and CEO**

Thank you.

**Operator**

And we have one final question from Morris Ajzenman with Griffin Securities. Please state your question.

**Q:** Hi, guys. I'll make it quick. Infrastructure, you touched on the previous question, 80% capacity utilization. Then earlier in the conversations, you spoke about the adjusted gross margins in infrastructure being 21.9 versus 22.8. First, is that correct? And secondly, if it is correct, why with the strength you've been experiencing in this division are the gross margins still at that level and actually down year-over-year? Shouldn't they be much higher? Can you just comment on that please?

**David C. Silvius - VP, CFO and Treasurer**

Hey, Morris. This is David. When Ben mentioned that, he was talking about 21.9% ex-pellets in Q3 of 2017, and he used the 22.8% number. That includes pellets last year, which had like a good profit in them in last year in the Infrastructure Group. But in the Infrastructure Group last year, ex-pellets, the gross margin was 19.7%. So really the 21.9% is a comp to 19.7% as opposed to the 22.8%, but I think he was just expressing the fact that even without pellets this year we were comparable too with pellets last year, but the true comp is 21.9% versus 19.7%.

**Q:** I appreciate the commentary, but again, 21.9% with the strength you are experiencing, I know you want to be at 25% gross margins or thereabouts for the company. You find that disappointing at this point or do you expect that to rise?

**Benjamin G. Brock - President and CEO**

Morris, one of the issues—this is Ben. One of the issues you ran into at Astec, Inc. is they ramped up for more pellet plant work, and we have had a reduction in force at Astec, Inc. So we had a higher cost basis than we needed for the asphalt plant business. And so that showing up in our margin is where you're seeing that. I think you'll see an increased margin, ex-pellet margin going forward in the Infrastructure Group.

**Q:** Thank you.

**Operator**

Ladies and gentlemen, we have reached the end of our question-and-answer session. I would like to turn the call back to management for closing remarks.

**Stephen C. Anderson - VP, Director of IR and CS**

Thank you, Sherry. We appreciate your participation on this third quarter conference call and thank you for your interest in Astec. As our news release indicates, today's conference call has been recorded. A replay of the conference call will be available through November 7, 2017, and an archived webcast will be available for 90 days. A transcript will be available under the Investor Relations section of the Astec Industries website within the next seven days. All of that information is contained in news release that was sent out earlier today.

So again, this concludes our call. Thank you, all. Have a good week.

**Operator**

Thank you. You may disconnect your lines at this time, and thank you for your participation.