Summit Materials

Fourth Quarter 2019 Earnings Conference Call

February 5, 2020

CORPORATE PARTICIPANTS

Karli Anderson, *VP, Investor Relations*

Thomas Hill, *Chief Executive Officer*

Brian Harris, *Chief Financial Officer*

CONFERENCE CALL PARTICIPANTS

Rohit Seth, *SunTrust*

Trey Grooms, *Stephens*

Philip Ng, *Jefferies*

Stanley Elliott, *Stifel*

Anthony Pettinari, Citigroup

Michael Dahl, *RBC Capital Markets*

Robert Whitworth, *Exane BNP Paribas*

Brian Biros, *Thompson Research Group*

Froylan Mendez, *JPMorgan Chase & Co.*

Brent Thielman, *D.A. Davidson & Co.*

Seldon Clarke, *Deutsche Bank*

Garik Shmois, *Loop Capital Markets*

PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the Summit Materials' Fourth Quarter 2019 Earnings Conference Call.

At this time all participants are in a listen-only mode. After the speaker’s presentation there will be a question-and-answer session. To ask a question during the session, you will need to press star, one on your telephone. In order to allow time for everyone to ask a question today, please limit yourself to one question and one follow-up. If you have additional questions, please re-enter the queue.

Please be advised that today's conference is being recorded. If you require any further assistance, please press star, zero.

I would now like to hand the conference over to your speaker today, Karli Anderson, VP of Investor Relations. Thank you. Please go ahead.

Karli Anderson, *VP, Investor Relations*

Welcome to Summit Materials' Fourth Quarter and Full year 2019 Results Conference Call.

We issued a press release this morning detailing our financial and operating results. This call is accompanied by our fourth quarter and full year 2019 investor presentation and an updated supplemental workbook highlighting key financial and operating data, all of which are posted to the Investors section of our website.

Management's commentary and responses to questions on today's call may include forward-looking statements, which by their nature, are uncertain and outside of Summit Materials' control. Although these forward-looking statements are based on management's current expectations and beliefs, actual results may differ in a material way. For a discussion of some of the factors that could cause actual results to differ, please see the Risk Factors section of Summit Materials' latest annual report on Form 10-K, which is filed with the SEC. You can find reconciliations of the historical non-GAAP financial measures discussed in today's call in our press release.

Today's call will begin with remarks from Tom Hill, who will provide an update on our business and then Brian Harris will provide a financial review, and Tom will finish with an update on our management outlook. At the conclusion of these remarks, we will open the line for questions.

With that, I'll turn the call over to Tom.

Thomas Hill, *Chief Financial Officer*

Good morning, everyone, and thank you for joining our call.

Turning to Slide 4 of the presentation.

Summit had an outstanding year with volume and price growth in all lines of business. We set records for annual net revenue, Adjusted EBITDA and free cash flow. Our full year results were favorably impacted by a surge of activity in our aggregates business late in the fourth quarter related to flood repair work in our East region as well as improved weather conditions in our largest markets.

There was a significant rebound in our results in 2019, much of which is due to strong organic growth. When making year-over-year comparisons for both the fourth quarter and full year, it's important to also remember that Summit confronted challenging weather and market conditions in 2018, from which I believe we emerged a stronger company.

Net revenue topped $2 billion for the first time in Summit's history, an increase of 6.4% relative to a year ago. Net revenue was up 13.7% in Q4 over the prior year period. This increase in net revenue was a function of higher price and volume, particularly in aggregates and products.

Operating income increased to $213.6 million in 2019, up 31.4%. In Q4, operating income more than doubled from a year ago to $59.9 million. Operating margin expanded to 10.5% in 2019 from 8.5% in 2018 as net revenue grew faster than our costs.

Net income increased to $59.1 million in 2019, up 74% from a year ago on higher net revenue and organic growth.

Adjusted EBITDA grew 13.6% in 2019 and 29.6% in Q4, reflecting organic price and volume growth in all lines of business stabilizing variable costs and improving weather conditions. We increased our Adjusted EBITDA margin by 140 basis points to 22.7% for the full year.

In 2019, we focused on growing our top line, controlling variable costs, managing working capital and allocating resources more efficiently. This disciplined approach resulted in record free cash flow of $180.9 million. We ended the year with over $300 million in cash on the balance sheet, and we reduced our net leverage ratio to 3.6x, which is almost one full turn improvement from a year ago.

Turning to Slide 5.

Now I'll give you more details on our 2019 operating performance and 2020 outlook. Pricing was very positive with growth in all lines of business. Summit's organic pricing growth was led by aggregates, which increased 6.5% from a year ago. On a mix adjusted basis, aggregates pricing increased 4.4%. Asphalt pricing was another bright spot, up 6.2% over last year on strength in our Utah, Texas and Kentucky markets. We believe that 2019 pricing reflected strong demand for building materials as well as a catch-up to the industry-wide cost increases that occurred in 2018.

Looking forward to 2020, we expect mid-single digits price increases in aggregates and ready-mix, and we are cautiously optimistic on Cement pricing. We expect to have better visibility into Cement pricing in the second quarter.

From a volume standpoint, 2019 was an outstanding year. Organic aggregates volumes were up 9.5%, reflecting the contribution from flood repair work and higher public demand in several of our markets. On a mix adjusted basis, aggregates volumes increased by approximately 6%. Our outlook for 2020 calls for low single-digits volume growth in all lines of business. Our outlook also assumes that weather conditions in 2020 will be similar to those in 2019.

Our focus on variable cost management intensify as 2019 progressed as we look to offset the impact of some operational challenges with better efficiency. This included our ongoing efforts to implement lean processes, labor cost management practices and purchasing improvements. In 2020, we expect to reap benefits from some of our performance improvements initiatives as we expect them to positively influence cost. However, we also expect some cost headwinds in the form of higher benefit and insurance premiums.

In 2019, we saw a meaningful improvement in adjusted gross profit margins in aggregates, products and services while our Cement gross margin contracted on higher distribution costs due to barge traffic closures. In 2020, we'll focus on further margin improvements through sustained price enhancement in all lines of business, proactive variable cost management and our performance initiatives.

Turning next to our outlook by end markets on Slide 6.

Single and multifamily construction indicators have improved over the last few months, providing for a cautious but healthy outlook for 2020. For example, December 2019 single-family housing starts were 1.1

million units, the highest level since 2007. Supply and homeownership remain well below their peaks and historical averages.

Employment, interest rates and affordability indicate a growing housing market in the near term. We expect solid residential demand in our largest markets, such as Texas and Utah, where consumers continue to purchase homes at affordable prices.

In the non-residential sector, Summit continues to experience moderate growth as we focus on low-rise commercial construction, that tends to follow residential development.

After a soft start to 2019, architectural billings increased late in the year, led by the Southwest and Midwest markets. This data point rings true with Summit as we see low-rise commercial and wind farm projects continuing to present opportunities for growth.

Looking to the public market. ARTBA is forecasting 6% growth in 2020. Statewide initiatives to boost funding for transportation, construction and repair, enjoy broad support. On a national basis, 89% of state and local transportation investment ballot measures were approved in the November 2019 election. Overall, ARTBA forecasts a 2.6% CAGR for U.S. highway, bridge and related construction spend through 2024.

There is an update on our Greenfield strategy on Slide 7.

Aggregate Greenfields enable Summit to enhance its position in high-growth markets, add reserves and generate incremental Adjusted EBITDA in areas where acquisition opportunities are limited. Our projects focus primarily on the Southeast and Western U.S. We currently have five projects completed and three in development. We estimate that these projects will add 450 million tons of reserves on an annualized basis, generate shipments of 7 million tons of aggregates.

Spending on Greenfields from 2014 to 2018 was about $90 million. We spent about $25 million in 2019, expect another $65 million to $80 million in 2020 and a further $10 million to $15 million in 2021. Importantly, these Greenfields offer entry into markets that may be unavailable through acquisition alone and at an upfront investment far below the prevailing rate of pure aggregates operations of scale of up to 15x EBITDA. At run rate EBITDA levels our Greenfield investments represents a purchase multiple of EBITDA, which is less than half of these high current market values.

Our chart on Slide 7 shows an estimate of the growth and incremental Adjusted EBITDA from these active Greenfields. In 2020, we estimate the total contribution is about $15 million, which is embedded in our 2020 outlook. We expect the Greenfield's contribution to grow to $45 million of Adjusted EBITDA by 2024. It can be difficult to estimate the specific timing of Greenfields because their development is subject to permitting time frames, well beyond our control as well as the site development, delivery and commissioning of equipment. The chart on Slide 7 is our best estimate at this time. We're also working on many projects to add to this list as time goes on.

With that, I'll turn the call over to Brian for a discussion of financial results.

Brian Harris, *Chief Financial Officer*

Thank you, Tom.

As I discuss the financial results for both the fourth quarter and full year 2019, I'll second Tom's introductory comment that our relative outperformance in Q4 and full year 2019 reflects a combination of strong organic growth as well as a return to a relatively normal operating and market conditions after a difficult 2018.

Turning to Slide 9.

We have our full year net revenue bridge comparing 2019 to 2018. Net revenue increased 6.4% and was led by our East region, which contributed an incremental $82.1 million, much of which can be attributed to higher public market activity and improved weather conditions towards the end of the year. In the West segment, organic net revenue increased by $41.2 million, but was offset by the sale of a non-core business in the third quarter of 2018 of roughly the same proportion.

Turning to Slide 10.

You'll see the year-over-year Adjusted EBITDA bridge. Our 2019 result is up 13.6% from 2018. The increase was driven primarily by organic growth in the East region as well as an incremental contribution of organic growth in the West region, where improved weather conditions added more working days towards the end of the year.

Turning to Slide 11.

You'll see the key GAAP financial metrics. Net revenue increased 13.7% for the fourth quarter and 6.4% for the year on higher volume and price increases in all lines of business. Our East segment was the largest incremental contributor, while our Cement and West segments also delivered moderate net revenue growth.

Operating income more than doubled in the fourth quarter of 2019 as compared to the fourth quarter of 2018. For the full year 2019, operating income increased 31.4% to $213.6 million as pricing and volume gains exceeded the cost of revenue. Reported net income attributable to Summit, Inc. was $35.7 million for the fourth quarter and $59.1 million for the year.

Turning to Slide 12.

We've presented several non-GAAP financial metrics. Adjusted cash gross profit margin expanded by 390 basis points in Q4 2019 and 160 basis points for the full year 2019 as a result of higher average selling prices and volumes in all lines of business.

Adjusted EBITDA margins expanded by 290 basis points in the fourth quarter 2019 and by 140 basis points for the full year on higher net revenue, due primarily to organic growth in our aggregates business.

Adjusted diluted net income increased $90.2 million and $91.4 million in the fourth quarter and year ended 2019, respectively, due to higher revenue and the remeasurement of our TRA liability, which was favorable to adjusted earnings.

Turning to Slide 13.

We've provided a comparison of our price and volume in 2019 relative to 2018. On an organic basis, average selling prices increased 6.5% for aggregates and 1.7% for cement. As we said on our last two earnings calls, we expected some upward movement on average cement selling price as business picked up towards the northern markets and weather conditions improved. Cement pricing continues to reflect the competitive environment, and we expect to have more visibility into 2020 pricing in the second quarter.

Aggregates volumes increased 9.5% in 2019 as flood repair work, higher public market activity and favorable weather conditions resulted in strong demand for our products. Cement volumes increased 2.8% in 2019 as strong demand from northern markets and at our new Memphis terminal was balanced with more moderate demand trends in the Midwest, some of which was related to the challenging agricultural end market.

Ready-mix volumes were flat in 2019, and Asphalt volumes were up 2.6%, while prices increased 3.3% and 6.2%, respectively.

Turning to Slide 14.

We are making good progress on margin recovery with 2019 adjusted cash gross margins in our Aggregates, Products and Services lines of business above 2018 levels. Notably, our Aggregates gross margins expanded by 80 basis points, and our Services line of business expanded by 120 basis points over 2018. However, we remain below historical highs and believe there is scope for further margin expansion.

In our Cement segment, higher distribution costs adversely affected our adjusted cash gross profit margin by approximately 4%. Materials and products now comprise 89% of our adjusted cash gross profit. We expect the contribution from Aggregates and Cement to be an increasing proportion of our adjusted cash gross profit margin.

Turning to Slide 15.

You'll see a summary of our capital expenditures for 2019. There is a chart depicting our capital expenditures as a percentage of net revenue, which is returning to our target of 7% to 8% without the impact of Greenfields. Including Greenfields, total cap ex was about 9% of net revenue.

In light of our very strong operating cash flow, we reduced our leverage by nearly a full turn at year-end 2019. Our net leverage at the end of the year was 3.6x, well below our guidance of less than 4.0x.

For quarterly modeling purposes for 2020, SG&A should be in a range of $70 million to $73 million, DD&A should be in the range of $53 million to $55 million and interest expense should be in the range of $29 million to $30 million. We anticipate paying minimal state and local cash taxes and no U.S. federal income taxes. In addition to minimal cash taxes, we do not expect to have any significant TRA payments until 2025.

Finally, with regards to total equity interest outstanding, we had 113.3 million class A shares outstanding and 3.3 million LP Units held by investors, resulting in total equity interest outstanding of 116.6 million at year-end 2019. This is the share count that should be used in calculating the adjusted diluted earnings per share.

With that, I'll turn the call back to Tom for his closing remarks.

Thomas Hill, *Chief Financial Officer*

Thank you, Brian.

Turning to Slide 17.

I'd like to put some additional context around today's results and our 2020 guidance. Last October, we narrowed our 2019 guidance to $440 million to $460 million of Adjusted EBITDA. We had a strong finish to 2019 and surpassed the high end of that guidance.

Our 2020 outlook reflects limited visibility at this early point of the year into several factors, such as cement pricing, weather conditions and the level of flood repair work. These factors present both risks and opportunities.

Given that we are still early in the year, we want to be careful to allow ourselves the opportunity to make additional refinements to our guidance once we have more clarity on market and weather conditions.

Our 2020 Adjusted EBITDA guidance is $460 million to $500 million. The high end of this range represents 8% year-over-year growth. Our guidance is based on these current assumptions.

First, we expect that Aggregates will have low single-digits volume growth and mid-single digits price growth.

Second, we expect that Cement will have both low single-digit volume and price growth.

Finally, we expect that our products and services businesses will exhibit slight margin improvements. As we've mentioned, cement pricing, weather conditions and the level of flood repair work could have a significant impact on our 2020 results.

We estimate 2020 capital expenditures to be in the range of $185 million to $205 million, inclusive of $65 million to $80 million for Greenfields. Assuming the midpoint of our guidance, we expect to end 2020 with a net debt-to-EBITDA ratio in the low 3s.

Concluding on Slide 18.

Summit is starting 2020 from a position of strength. Our financial ratios have vastly improved from a year ago. We have delevered by nearly one full turn to 3.6x, and we expect to delever through further cash generation and Adjusted EBITDA growth.

Our cash flow return on invested capital is 10.2%, matching our record level achieved in 2016. We're focusing on margin expansion. We plan to return to and ultimately exceed historical adjusted gross profit margins in all of our lines of business.

Our December backlogs increased 12% in Aggregates, 32% in Asphalt, 34% in Ready-mix and 31% in Paving relative to a year ago. Solid backlogs are indicators of healthy underlying end markets.

Our Greenfields program is generating Adjusted EBITDA, and it is providing a nice complement of growth to our existing portfolio. Our end market indicators are strong with rising housing starts, growing household formation and bipartisan support for public road construction and repair.

Our M&A pipeline remains active, and we will always be at the table to consider new opportunities carefully evaluating them in the context of maximizing value for our shareholders, and finally, there is a positive outlook in the construction cycle.

I want to thank all of our employees for their dedication and contribution to our rebound from the challenges of 2018 to the record net revenue, Adjusted EBITDA and free cash flow that we are reporting today. We will continue to focus on providing a safe work environment for our employees, and as always, we are committed to generating value for our shareholders.

With that, I'd like to turn it over to the operator for questions. Operator?

Operator

As a reminder, to ask a question, you may press star, one on your telephone. To withdraw your question, please press the pound or hash key. In order to allow time for everyone to ask a question, please limit yourself to one question and one follow up. If you have additional questions, please re-enter the queue. Please standby while we compile the Q&A roster.

Your first question comes from Rohit Seth with SunTrust.

Rohit Seth, *SunTrust*

Hi. Thanks for taking my question. Just on your annual guidance, you provided some good color on the slide deck. I just want to expand on a few of the assumptions. Can you talk about your margin expectations by product line and does the guidance include Cement price realization? Then just curious on the SG&A guidance, it looks like a significant increase. Maybe just you can comment on the driver there.

Thomas Hill, *Chief Executive Officer*

Yes. Thanks, Rohit. Yes, we expect to have continued margin expansion basically across the board. Cement pricing, we're looking at low single digits, and we would hope to exceed that, but that's certainly what we have in our guidance. Brian, do you want to talk about SG&A guidance?

Brian Harris, *Chief Financial Officer*

Yes. The SG&A guide that we've given does include the stock comp on a reported basis, we add that back for Adjusted EBITDA. I think it's generally moving in line with underlying inflation trends. A lot of the SG&A is wage and salary that runs at about 3%, so that's kind of the expectation that we have. We're seeing a little bit more elevated levels of cost in things like insurance premiums, but otherwise, broadly in line with inflation.

Rohit Seth, *SunTrust*

Okay. Because I'm seeing a disconnect from the bottoms-up assumptions and what the annual guidance range is. It seems like when I put these low single-digit volume, mid-single digit price assumptions in my model, I'm coming out at the high end of your range. I was just curious is there any—I'm just trying to bridge the gap there on your $460 million to $500 range. Anything I'm missing on this?

Thomas Hill, *Chief Executive Officer*

Well, I think the major one is that, look, the weather in our market area has been unprecedented from the end of '17, all the way through the midpoint of '19. The weather in the second half of '19 was better, still not great, but a little better. So the weather impact on our 2018 results has certainly left us a bit cautious. So really, until we see definitive proof that the weather patterns have changed, we're going to be conservative in our guidance, and that's really the underlying cause for the guidance to be where it is.

Rohit Seth, *SunTrust*

All right, I'll get back in queue. Thanks.

Operator

Your next question comes from Trey Grooms with Stephens. Your line is open.

Trey Grooms, *Stephens*

My first question here is kind of still around the guidance. I get conservatism totally and I appreciate that. But if we're looking at this and kind of what the organic growth assumptions are and what it would take to get to the different parts of the range that you've given us, on the low end, it looks like you'd have to actually have negative organic growth. So I guess, I'm trying to get at—the midpoint seems like basically flat organic growth and then from there down is something less than flat. So I guess, within that—I guess, what scenarios had to play out for you to see something below that midpoint, something closer to the low end, where you're seeing actual organic EBITDA turn negative or the growth turn negative?

Thomas Hill, *Chief Executive Officer*

Yes. Thanks, Trey. I think at the midpoint, though, it's more like a 4% organic. But really, there's three major risk areas that we have going into 2020. It's weather, cement pricing and the amount of flood repair work that we have in the middle part of the country on the Mississippi and Missouri River areas. The cement pricing and the flood repair work, we really don't have any control of and we really don't have any visibility on it at this part of the year. All of those areas all have to go negative for us to be at the low end of our range. If we get good weather, if we get decent weather, we should be up towards the top end of the range. But like I say, 2018, we saw negative organic growth basically due to weather and that's sort of left us very cautious.

Trey Grooms, *Stephens*

Just for clarity, Tom, you said 2020 guide implies weather similar to '19. If I heard that correctly, is that kind of the midpoint kind of base case is the repeat of '19, it's kind of weather events?

Thomas Hill, *Chief Executive Officer*

Yes. And I would look at 2019 in total has worse than normal weather. The first six months of 2019 were a continuation of sort of the unprecedented weather that we had from the end of '17. The second half of the year was okay. Wasn't great, to be honest, but it was just significantly better than what we experienced in the second half of '18. You just hope to see a change in the weather pattern.

Trey Grooms, *Stephens*

Got it. Okay. That's all super helpful. Then as a follow-up, would be on the Cement business in the quarter, volume came in a little lighter than what we were looking for. Anything in the quarter to kind of point out to kind of drive that underperformance relative to some of the other lines of business there.

Thomas Hill, *Chief Executive Officer*

Yes. I mean cement, in general, had three major issues. They had just terrible weather. I think the weather in Minneapolis, which is our largest cement market, was the worst in recorded history and we also had some unplanned outages earlier in the year. Then of course, we had the lock—the river closures. We certainly, in the quarter, had continued increased logistical costs due to those shutdowns. The underlying demand that we believe in our cement markets is pretty good and what we need is just the ability to get the weather to fill the demand.

When I look at our Cement business, I look in 2020, I think demand should be good. Utilization of ours and our competitors should be slightly higher. The industry has come out with an $8 a ton price increase. And in normal times, you would get a significant amount of that in your realized price. So there's no reason our Cement business can't do significantly better than it did in '19. But we've had a couple of rough years in Cement, so we're also being cautious there.

Trey Grooms, *Stephens*

Got it. But just kind of for clarity on the question was more around kind of the volume in cement being pretty flat in 4Q. Was there anything specific, and you may have answered it, and it may just kind of boil down to weather and things like that. But just specifically in the 4Q, was there anything to note on the volume being rather flat?

Thomas Hill, *Chief Executive Officer*

Pretty poor weather in the northern part of the Mississippi River system.

Trey Grooms, *Stephens*

Okay. That does it for me. Thanks guys.

Thomas Hill, *Chief Executive Officer*

Thanks Trey.

Operator

Your next question comes from Philip Ng with Jefferies.

Philip Ng, *Jefferies*

When we think about some of the cost headwinds you've incurred in Cement and certainly dredging costs in Agg. How much of that is behind you at this point and anything that could be incremental in 2020?

Thomas Hill, *Chief Executive Officer*

Certainly on the Aggs, the dredging is behind us. We had a dredge that sank. We have a replacement dredge and they're running and is running quite well. So I believe that, that's behind us and certainly should be incremental in 2020. We expect to have a better year in Cement as far as how are Cement plants are run. We did have some unusual events last year. So I think on both of those, we should see some incremental improvement in 2020.

Philip Ng, *Jefferies*

Okay. Are you expecting the issues that you saw in Cement pretty much behind you at this point or it's still kind of a work in progress?

Thomas Hill, *Chief Executive Officer*

I think on the cost side, they should all be behind us. The big variable there for us is—well, two variables. One is demand, and two is cement pricing going to return to a more rational, thoughtful market. That's, I think, the two variables that we have to look for.

Philip Ng, *Jefferies*

Got it. Just one final one on that. I mean if you look at—if we assume low single-digit growth in your Cement business in 2020, you should be getting pretty close to being sold out. I noticed you incurred some warehouse costs in the fourth quarter. Are you building a little inventory ahead of the year? And ultimately, do you have enough capacity to kind of meet this demand this year?

Thomas Hill, *Chief Executive Officer*

Yes. I mean, we're basically sold out, and we always build inventory this time of year to service the busier season. I must say, if I look back, we would have expected to have been importing a few hundred thousand tons of cement at this point. So we're disappointed on the demand as well as the price in our cement business and we have a great cement business, very well run, very high margin, great logistics, but it's been a tough couple of years. So we would expect to return to more normal operations in 2020.

Phillip Ng, *Jefferies*

Okay. Great color. Hopefully, rainfall out, leads to better pricing. Thanks a lot.

Thomas Hill, *Chief Executive Officer*

Okay. Thanks Phillip.

Operator

Your next question comes from Stanley Elliott with Stifel.

Stanley Elliott, *Stifel*

Good morning guys. Thank you for taking the question. With the leverage coming down, kind of closer to three by the end of next year, can you talk a little bit more about your thoughts around M&A? This will be the lowest leverage, I think, since you guys have been public. I'm curious to see what the outlook looks like there, even though you talked about a pretty full pipeline versus what you're doing now on the Greenfield side?

Thomas Hill, *Chief Executive Officer*

Yes. I mean we're very active on the M&A side. Lots of good, small deals anywhere from $10 million to $100 million, would be very disappointed if we didn't complete a few of those. There have been a few larger transactions out there that we looked at, but just couldn't make sense of the prices. So we passed on those. But no, I'd be very optimistic about being back into the M&A business here in the short term.

Stanley Elliott, *Stifel*

Just to make sure that's not included in the current outlook.

Thomas Hill, *Chief Executive Officer*

It is not. We never put any M&A in the outlook.

Stanley Elliott, *Stifel*

That's what I thought, just to clarify. Then Brian, would you care to tackle kind of anything on the seasonality with this year coming up, it's going to be difficult in terms of kind of the weather piece from last year and then a little bit of a stronger second half. Is there anything that you want to convey to us as we're making our models public or anything along those lines?

Brian Harris, *Chief Financial Officer*

Yes. I'd say the first half of 2019 was obviously quite a difficult period, the weather was still poor and obviously, we had the issues with the flooding on the Mississippi. So I'd say, first half would be the easier comp of the two halves. Then the second half, obviously, we've had a strong finish to the year in Q4. Q3 was pretty strong with good margins across the board. So second half would, therefore, likely be a little bit more challenging from a comp perspective.

Stanley Elliot, *Stifel*

Perfect guys. Thanks for the time.

Operator

Your next question comes from Anthony Pettinari with Citigroup.

Anthony Pettinari, *Citigroup*

Good morning. Tom, I was wondering if you could talk a little bit more about the levy work and flood repair activity that you saw in the quarter sort of relative to your expectations? How much further do you see that continuing into 2020? Then with regards to the guide, I mean, I think we can kind of back into the weather and potential cement price impact. Is there any kind of quantification on how much of a swing factor, flood repair work could be with regards to the 2020 guide?

Thomas Hill, *Chief Executive Officer*

The flood repair work consists of three major areas. The amount of devastation on the Mississippi and Missouri River systems was absolutely amazing when you go out and see it and destroyed hundreds of miles of country roads, hundreds of miles of rail and also a lot of the levies were destroyed. So aggregate goes into all three of those areas.

We said at the end of Q3 that the levy work would more than offset the shortfall in our Cement business, and that is really what happened in Q4. We're not going to quantify it. But I will say you know that we have a small backlog in flood repair work going into 2020 and e expect to pick up a bit more, but it's really unpredictable. Anthony, it's core of engineer. We'll call you on Monday and tell you to start shipping on Friday. It's really tough to determine how much that would be. So there's probably some upside and some downside on the flood repair work. I suspect that flood repair work will go on for years because there's just—I say the devastation, unless you've seen it, it is pretty hard to comprehend.

Anthony Pettinari, *Citigroup*

Okay. That's helpful. Then I think in the outlook, you said you're expecting mid- single-digit pricing in Aggregates and RMC and you're cautiously optimistic on Cement. Apologies if I missed this, but anything you'd call out specifically on asphalt pricing?

Thomas Hill, *Chief Executive Officer*

No. We didn't and typically, pricing in asphalt is not that important a factor because you're really focused on margins just because the type of liquid asphalt that goes into the asphalt can swing the price up and down dramatically. So really, we focus on margin, and I think we did call out that we expect margins to be slightly better in 2020 in asphalt than in '19. So we don't really focus on price. Obviously, we always want it to be up. But it's really not a determining factor on margin as much as in the other business lines.

Anthony Pettinari, *Citigroup*

Okay. That's helpful. I'll turn it over.

Thomas Hill, *Chief Executive Officer*

Thank you.

Operator

Your next question comes from Mike Dahl with RBC Capital Markets.

Michael Dahl, *RBC Capital Markets*

Hi. Thanks for taking my questions and the commentary so far. First question, just wanted to go back to kind of the Aggs volume guide and then talk more about the Greenfields. I guess just to clarify or confirm, are the Greenfields included in the low single-digit volume outlook? Because at least rough math, I would think that Greenfields alone, if you're talking to $15 million of incremental EBITDA translates to 2% to 3% on the volume side. So that alone gets you to low single digits and outside of the flood swings. Just wondering if there's anything else we should be considering there.

Brian Harris, *Chief Financial Officer*

Yes. Mike, it's Brian here. The Greenfield $15 million is not incremental. It's up a little bit from 2019, but you should not consider that to be all incremental.

Michael Dahl, *RBC Capital Markets*

Got it. Okay. That helps. Then secondly, on Cement, I think last quarter on some of the headwinds that you've discussed, you had outlined an expectation that in aggregate, those would cost you about $12 million between the floods and some of the winter shutdowns. It sounds like maybe that came in a little higher in the fourth quarter than expected. But just wondering if you can give us an update on what that ended up costing you for the full year in '19?

Thomas Hill, *Chief Executive Officer*

It probably did come in slightly higher, maybe up to $2 million higher. But again, the flood repair work more than offset that, and actually between the 2, ended up in a positive net effect on our results in the Q.

Michael Dahl, *RBC Capital Markets*

Got it. Okay. Thanks.

Operator

Your next question comes from Paul Roger with Exane BNP Paribas.

Robert Whitworth, *Exane BNP Paribas*

Hi gents. This is actually Robert Whitworth on for Paul Roger. I wanted to start by asking, as you mentioned earlier, the industry has announced was put forth an $8 per ton price increase in most states. I just wanted to know what visibility do you have that it could stick, and just how are conversations going with customers, for example?

Thomas Hill, *Chief Executive Officer*

Conversations with customers are very positive. It's just very early days, Robert. In normal times, you would expect to get $5 or $6 of that in realized price. We have not gotten that in the last couple of years. So that's where the cautiously optimistic comes from. We hope that the industry returns to more rational approach, and we should have more success on our cement price, but I think it's just too early. It's really when the the price increase takes effect April 1. It's really into late March and April and really the 1st of May before you actually know what part of that is going to stick.

Robert Whitworth, *Exane BNP Paribas*

Great. Thank you. Just as a follow-up, I wanted to note, did your ready-mix volumes in Texas and Utah benefit from any one-off contracts? Why do you expect demand growth to slow in 2020?

Thomas Hill, *Chief Executive Officer*

I don't think we had any—we actually had a big project in '18 that impacted the '19 comp in Salt Lake City at the airport. No big projects come to mind. Our volumes in Utah were impacted by a very late spring wet cold spring, and we just couldn't catch up. Excuse me, Robert, what was the second part of your question?

Robert Whitworth, *Exane BNP Paribas*

It was just around why do you expect demand growth to slow in 2020 just in terms of ready-mix volumes?

Thomas Hill, *Chief Executive Officer*

Ready-mix volumes would be low single digits increase. We see the market's quite strong. Actually, it's more of a residential business than most of our businesses and residential is strong. I mean in Utah, our biggest constraint is labor, both from our customers and filling all of our ready-mix trucks. So that probably constrains the growth. But no, we should have good solid years. If the weather improves in Houston, we could see significant upside in volume there because whenever the sun shines there, we are very, very busy.

Robert Whitworth, *Exane BNP Paribas*

Very helpful. Thank you.

Operator

Your next question comes from Kathryn Thompson with Thompson Research.

Brian Biros, Th*ompson Research*

This is actually Brian Biros on Kathryn. I want to ask on the Cement segment, if you guys could provide any additional color on the nature of the unplanned maintenance in the quarter and I guess, if that has any impact on the magnitude or cadence of routine maintenance in 2020?

Thomas Hill, *Chief Executive Officer*

No. The unplanned shutdowns were earlier in the year. We had a very fluky fan disruption that knocked us down for a number of days. But there was nothing really in the quarter. We have normal shutdowns planned in February and March in both our plants, somewhere between two and three weeks at each plant. We're getting very close to one of them, I think, Hannibal starts, what, in a couple of days and then Davenport starts at the end of the month. So really, nothing unusual in the 2020 shutdowns.

Brian Biros, *Thompson Research*

Got it. And a quick follow-up, I guess, some of our industry contacts have shared with us that the Denver market, specifically seeing better housing trends for 2020 kind of after a pause in 2019, I think, mostly driven by just affordability. I just want to see if you guys are seeing a similar trend in the Denver market, or if there are any other geographies that you would call out on the residential side?

Thomas Hill, *Chief Executive Officer*

Although our headquarters are here in Denver, we don't have any operations. So we really have no insight into the Denver market. Our major ready-mix markets are Salt Lake City and Houston. In both those markets, our customers are very optimistic after coming off of good '19 that they should see some continued growth into '20. The statistics as far as the amount of inventory affordability, interest rates, everything points to a very positive underlying residential market.

Brian Biros, *Thompson Research*

Got it. Appreciate it.

Thomas Hill, *Chief Executive Officer*

Thanks Brian.

Operator

Your next question comes from Froylan Mendez with JPMorgan.

Froylan Mendez, *JP Morgan*

Hi guys. Thank you very much for taking my question. Regarding the cement market, how have your market share change after the tough 2019 for logistics? Is there any market that you weren't able to serve that you could potentially recover this year?

Thomas Hill, *Chief Executive Officer*

Not really. Our team there did an absolutely masterful job of supplying our customers, albeit at a pretty significantly higher cost, but we did okay in supplying our existing customers. Market shares really didn't shift in '19. What we need to see is just some underlying market growth and we're optimistic that we'll see that in 2020.

Froylan Mendez, *JP Morgan*

Glad to hear that. Justas a follow-up from the previous question, how much was the EBITDA contribution from your Geenfields in the aggregate side during 2019, roughly?

Brian Harris, *Chief Financial Officer*

It was probably in the $12 million to $14 million range.

Froylan Mendez, *JP Morgan*

Thank you so much guys. Congrats on the results.

Thomas Hill, *Chief Executive Officer*

Thank you.

Operator

Your next question comes from Brent Thielman with D.A. Davidson.

Brent Thielman, *D.A. Davidson*

Okay. Great. And congrats as well. Tom, when you look at your energy tied (phon) kind of local markets, Permian and elsewhere, any signs of pause or slowdown there?

Thomas Hill, *Chief Executive Officer*

We're in Odessa/Midland, it's still very busy. We don't service the oil markets directly. We service the resin non-res, which services the oil business out there. We really haven't seen much of a slowdown at this point. It wouldn't surprise me if we do. But it's a relatively small part of our business. But right now, it continues to be quite busy.

Houston which is obviously still tied to the oil sector is really diversified dramatically. Great employment growth there in '19, expect it to continue into '20, just a very dynamic place. Affordability is fantastic on housing, lots of incoming business. Our customers, as I said earlier, our customers there are very optimistic about 2020.

Brent Thielman, *D.A. Davidson*

Okay. Then you guys, obviously, are putting some money into Greenfields in your markets and I'm going to kind of presume after a few good years in terms of the market, maybe some of the competition is doing the same. So I guess, when you kind of look around where you play, do you see anything or decisions competitively that causes you concern and maybe where adding capacity just doesn't make sense to you?

Thomas Hill, *Chief Executive Officer*

We've had a bit of that, a few years ago. We had a pretty aggressive entrant into the Austin market. That is still very competitive but is improving slowly. We have seen a couple of small asphalt entrants around the place, but nothing material, to be honest.

Brent Thielman, *D.A. Davidson*
Okay. Great. Thanks Tom.

Thomas Hill, *Chief Executive Officer*

Thanks Brent.

Operator

Your next question comes from Seldon Clarke with Deutsche Bank.

Seldon Clarke, *Deutsche Bank*

Just getting back to some of the earlier questions on the outlook for EBITDA margin in 2020 and just given all the moving pieces as you move from 2019 into 2020. But now that you're through the bulk of your M&A and given where you are in terms of scale, what's the right way to think about underlying operating leverage on a go-forward basis as as it relates to incremental EBITDA margins?

Thomas Hill, *Chief Executive Officer*

As far as incrementals?

Seldon Clarke, *Deutsche Bank*

Yes. I'm trying to get a sense of like how you think like now given where you are in terms of scale, like what the incremental margin should be on a kind of cleaner underlying basis?

Brian Harris, *Chief Financial Officer*

Well, gross margins, we've seen several quarters now, three in a row where we've been above 61%. Our highest this year was Q3 in aggregates, where we were 68%. We've always said that we'd like to get back to the kind of levels that we enjoyed in 2017. So we think about aggregates margins approaching the mid-60s. Cement margins were a little bit depressed this year, but largely as a result of the incremental cost for the extra downtime and the logistics that pulled us down by about 4%. Then the products margins, we're starting to track in the 22% to 25% range once we get into the mid-20s. There's probably a little bit less opportunity for significant margin expansion at that point. But we're now getting back into that range, again, back to those kind of 2017 levels where we were in the mid-20s.

Overall, EBITDA margins, again, we've been up very close to 25%, and that would be our goal would be to start to get back to that level. We're at about a little bit below 23% right now, an improvement over 2018, but further room for growth there as well.

Seldon Clarke, *Deutsche Bank*

Okay. Got it. That's helpful. Then did you guys give a free cash flow target for this year? I know you have EBITDA and cap ex, but anything else or as it relates to cash interest or working capital or some of the onetime items that you might expect in 2020?

Brian Harris, *Chief Financial Officer*

We did not provide any guidance on that.

Seldon Clarke, *Deutsche Bank*
Could you give any color on like how we should think about working capital or maybe one timers?

Brian Harris, *Chief Financial Officer*

Well, the working capital ratio pretty much stays fairly consistent year-to-year around about a 13% to 15% range. We've guided on our cap ex and our interest. The only other items to think about, typically, on the cash flow would be state and local cash taxes there in a $4 million to $6 million range. Deferred consideration on prior deals is going to be around about $30 million. So those are really the only other moving parts.

Seldon Clarke, *Deutsche Bank*

I appreciate the questions. Thanks.

Thomas Hill, *Chief Executive Officer*

Thanks Seldon.

Operator

Again, in order to allow time for everyone to ask a question today, please limit yourself to one question and one follow up.

Your next question comes from Garik Shmois with Loop Capital.

Garik Shmois, *Loop Capital*

Hi. Thanks for squeezing me. Just want to be clear on cement and cement pricing. I mean it sounds like your conversations with your customers thus far are encouraging. Is it fair to assume that really just outside of weather, is there anything else that gives you caution on the pricing landscape? Is the competitive landscape changing at all? Or I just kind of wanted to be clear on what's driving some of the, I guess, the lack of visibility on the Cement segment?

Thomas Hill, *Chief Executive Officer*

Well, certainly, in '18 and '19, we have what we believe was irrational behavior by one of our major competitors. That's probably the key variable for 2020, and we'll just wait and see.

Garik Shmois, *Loop Capital*

Okay. That's fair. And I guess, my follow-up is just on aggregates and aggregates margins. You had really good improvement in the fourth quarter compared to the prior fourth quarter. I think you also had in the middle of the year some deferred capital projects that you thought were going to (inaudible) that you were going to benefit. Did any of those deferred projects hit in the fourth quarter and is there any way to quantify what the potential benefit could be into next year?

Brian Harris, *Chief Financial Officer*

I think it's just the Greenfields, Garik, that we would have been referring to at that time in Q3. So we're going to get a little bit of incremental EBITDA from the Greenfields next year, but nothing too significant at this point. They're still ramping up. So no, there would be nothing else.

Thomas Hill, *Chief Executive Officer*

The new dredge, probably in North Texas, we'll see some incremental improvement on.

Garik Shmois, *Loop Capital*

Got it. Thanks.

Operator

This concludes our time for the question-and-answer session. I will now turn the call back over to presenters.

Thomas Hill, *Chief Executive Officer*

Thank you, operator, and thanks, everyone, for joining us today. That concludes our call. Everybody have a good day.

Operator

This concludes today's conference call. You may now disconnect.