

Transcript of
Lakeland Industries, Inc.
Lakeland Industries Fiscal 2023 First Quarter Financial Results and Conduct Conference Call
June 09, 2022

Participants

Charles Roberson - Director, Chief Executive Officer, President and Secretary, Lakeland Industries, Inc.

Allen Dillard - Chief Operating and Chief Financial Officer, Lakeland Industries, Inc.

Analysts

Alex Fuhrman - Craig-Hallum

Presentation

Operator

Good day and welcome to the Lakeland Industries Fiscal 2023 First Quarter Financial Results Conference Call. All lines have been placed on a listen-only mode and the floor will be opened for your questions and comments following the presentation.

During today's call, we may make statements relating to our goals and objectives for future operations, financial and business trends, business prospects, and management's future performance that constitute forward-looking statements under federal securities laws.

Any such forward-looking statements reflect management expectations based upon currently available information and are not guarantees of future performance and involve certain risks and uncertainties that are more fully described in our SEC filings.

Our actual results, performance, or achievements may differ materially from those expressed and or implied by such forward-looking statements. We undertake no obligation to update or revise any forward-looking statements to reflect events or developments after the date of this call.

During today's call, we will discuss financial measures derived from our financial statements that are not determined in accordance with U.S. GAAP, including EBITDA, adjusted EBITDA, and EBITDA margin. A reconciliation of each of the non-GAAP measures discussed on this call to the most directly comparable GAAP measure is presented in our earnings release.

At this time, I would like to introduce you to your host for this call, Lakeland Industries' Chief Executive Officer, Charlie Roberson. Mr. Roberson, the floor is yours.

Charles Roberson - Director, Chief Executive Officer, President and Secretary, Lakeland Industries, Inc.

Thank you, operator. Good afternoon and thank you for joining us on our fiscal 2023 first quarter earnings call. I'm joined today by Lakeland's Chief Operating and Financial Officer, Allen Dillard.

As you saw on this afternoon's press release, Lakeland delivered a solid quarter as we maintained our gross margin improvements and continued to execute on our strategic objectives. Our revenue for the first quarter was \$27.3 million, up slightly on a quarter-to-quarter basis. However, most importantly, we had strong profitability with a gross margin of 40.5%, which is in line with the long-term financial targets that we laid out in last quarter's call.

In terms of revenue, we believe that our topline results from the past two quarters inclusive of these most recent results constitute a revenue base from which we will continue to grow going forward with improved results in the second half of the fiscal year. We anticipate a pickup in demand across our end markets and are currently seeing strength return in the Fire Service and Electrical Utility segments of the broader energy markets.

While we have yet to see order rates returned to pre-pandemic levels in some of our important industrial markets, specifically the oil and gas segment, as we discussed in last quarter's call, we are beginning to see refinery turnaround scheduling for the second half of the year in Europe, and have been advised that activity in the U.S. market will also increase in the second half.

However, labor availability remains a challenge in the U.S. market, which has the potential to delay the process. More specifically with respect to this particular end market, we've seen various publications note the decline in the number of workers within the oil and gas segment, inclusive of extrication labor -- sorry, extraction labor, with employee levels down by approximately 100,000 workers as a result of the pandemic.

That said, we believe that turnarounds will increase in the second half of the year, albeit at a pace that the labor supply will support. We remain optimistic about a return to growth in these markets, and are increasingly positive that our operating leverage will be beneficial to our results as the demand comes back online.

Similar to others in our industry, we continue to face supply chain disruptions that pose risks to our business. Specifically as it relates to increasing freight costs and the ability to source and deliver our products.

Our team has done an outstanding job of mitigating these effects through strong inventory management and pricing actions. Quarter-to-quarter, we added approximately \$2.2 million in inventory as part of our planning to protect against potential future supply chain pressures on the business.

This is a continuation of our inventory strategy which we have accelerated since the beginning of the third quarter of last year as we believe product availability is critical to maintaining a high level of customer satisfaction and achieving our target gross margins.

It is also a significant competitive advantage relative to those in the industry who do not possess in-house manufacturing. Put more simply, our supply will be in Lakeland warehouses and not held up by raw material shortages or sitting in international ports in the event the freight supply chain becomes challenged in the future.

At the end of the day, we will have the product available and the ability to service our customer base in a timely fashion, which as we have stated before, is the one customer requirement that trumps price in our industry.

As it relates to our ongoing strategic initiatives, I will let Allen provide more detail. However, I'm pleased to say that our team has not taken our foot off the gas. This includes the build out of our sales and marketing team and investment in centralized data systems, manufacturing facilities, and new product development.

Looking ahead, I remain extremely confident in our team's ability to deliver on our long-term financial targets, which as a reminder include mid to high single-digit annual revenue growth on average in our core markets, gross margin levels in the low 40s, and EBITDA margin levels in the high teens to low 20s leading to strong and growing levels of free cash flow generation to further support our growth plans and priorities over the long-term.

That concludes my remarks. I'll now pass the call to Allen to provide more insight into the company's operations and financial results. Allen?

Allen Dillard - Chief Operating and Chief Financial Officer, Lakeland Industries, Inc.

Thanks Charlie and good afternoon, everyone. As Charlie highlighted, our results in the first quarter reflect the resiliency of the business model, our team has worked hard to refine as key profitability and operating metrics remain strong, despite headwinds outside of our control.

On a consolidated basis for the first quarter of fiscal '23, domestic sales were \$11.2 million or 41% of total revenues and international sales were \$16.1 million or 59% of total revenues. This compares with domestic sales of \$15.7 million or 46% of total revenues and international sales of \$18.4 million or 54% of total revenues in the same period of fiscal '22.

In terms of product mix for the quarter, on a consolidated basis, we saw essentially the same mix as we experienced in the fourth quarter last year, with disposables at 53% and chemical at 19% of sales. That said we did see some product mix shifts geographically with fire and wovens continuing to demonstrate strength in North America. We expect our product mix to rebalance towards disposables once we began to see increased U.S. industrial activity.

Distribution inventory continues to indicate it is correcting as our direct container order intake for future periods began to increase during the quarter. These orders are from our traditional industrial distributors, whose order rate has been depressed since the height of COVID demand in late 2020.

Gross profit as a percent of net sales was 40.5% for the fiscal '23 first quarter, down from 43.4% for the fiscal '22 first quarter. We continue to manage our raw material costs through proactive negotiations and longer-term purchasing arrangements.

Our production planning activities seek to balance reasonable manufacturing efficiencies and flexibility with our product inventory and stocking goals. We continue to be impacted by freight costs, but have been fairly successful in managing this via our pricing arrangements with our customers.

During the quarter, we were not impacted by curtailments in any of our manufacturing facilities and based on our manufacturing plan, expect to continue at normal capacity levels in the absence of unanticipated COVID interruptions.

Lakeland reported operating profit of \$1.4 million in first quarter '23, down from \$6.6 million in first quarter '22. Negative operating leverage for lower revenues versus the prior period as well as increases in travel and tradeshow expenses, administrative expenses and currency flux were the largest contributors to the drop in operating profits year-over-year. As a result, operating margins were 5.3% in the first quarter compared to 19.5% for the three months ended April 2021.

Net income was \$1.1 million or \$0.15 per common share down from \$5 million or \$0.63 per common share in first quarter of '22. Capital expenditures for the quarter were \$400,000. This figure compares to spending last year of \$800,000. The majority of our spending during the quarter was related to capital purchases for manufacturing facilities in Mexico, Vietnam, and India; expansion of our global IT infrastructure; and investments at our new corporate offices. We expect CapEx to be approximately \$3 million for the full fiscal year as we continue to make these adjustments and investments.

Moving to the balance sheet, working capital was a \$106 million at April 30, 2022 compared to a \$108.6 million at January 31, 2022. The company's current ratio at the end of the first quarter decreased to 8.1:1 from 12.8:1 at the end of the prior quarter, but it's up from 7.7:1 at the end of the first quarter of fiscal '22.

Our cash balance was \$50.8 million at the end of the quarter compared to \$52.7 million at the end of the fiscal year. The company continued to have no debt at the end of the quarter and has up to \$25 million available from bank credit facilities.

During the fiscal '23 first quarter, the company repurchased \$400,000 or just over 25,000 shares of common stock under its repurchase program. Notably, we were limited in our ability to buy back shares during the quarter as a result of a seasonally compressed trading window, which we experienced each year between the completion and reporting of our fiscal year end results and preparation for our fiscal first quarter reporting period.

However, in the shortened period that was available to us this past quarter, it's important to note we maximize our purchase activity for the days available in our open trading window. We now have approximately \$5.4 million remaining under the current authorization as of April 30, 2022.

Because of this, we expect to remain highly active in the market going forward, ultimately reaffirming our confidence in the company's future success.

As Charlie already alluded to, we remain committed to growing our market share, enhancing profitability, and focusing our efforts, our investments in areas that will drive attractive returns for our shareholders. For example, we are expanding our cleanroom manufacturing capabilities in Vietnam. Additionally, we are well down the road with a new manufacturing facility in Mexico that will not only expand our capacity in fire and woven products, but we'll also expand our capacity for nearshore opportunities in our traditional disposable market and cleanroom products.

Our investments in technology are expanding globally with CRM, planning, and reporting capabilities coming online in FY '23. These investments are expected to improve our decision-making and deliver operating efficiencies and support of our future growth initiatives.

With that overview, I'd like to turn the call over to the operator to open the call for questions.

Operator

Thank you. Ladies and gentlemen, the floor is now open for questions. [Operator Instructions]. And the first question is coming from Alex Fuhrman with Craig-Hallum. Your line is live.

Q: Hey, guys. Thanks for taking my question. Wanted to ask about the recovery of the oil and gas sector, it looks like revenue for the quarter was pretty nicely modestly above what you've reported the last two quarters and yet it sounds like oil and gas continues to be under pressure given the war and some of the labor constraints that you mentioned.

Can you talk about what you're seeing in the market that gives you confidence that oil and gas is going to be coming back in the back half of the year and have you started to see any signs of that yet? Or is this based on conversations with your customers, any more color, there would be very helpful.

Charles Roberson - Director, Chief Executive Officer, President and Secretary, Lakeland Industries, Inc.

The bulk of our oil and gas businesses here in the United States, and specifically Gulf Coast, and Southern California-oriented. And what we're garnering with regard to the second half is primarily talking to our distributors that are working with those end users.

They have pushed off maintenance longer than they would have liked to, labor is the primary constraint that everyone's trying to deal with now. So, it's likely that we're not going to see full turnarounds, but we're going to see individual parts of plants come down as labor's available. As far as why I think that it's going to happen in the second half, I think that the pricing for fuel is getting to where efficiency is going to matter. They're going to have to be able to produce more rapidly.

I think the supply side is being worked out. OPEC and OPEC+ just announced that they were increasing or Saudi announced that they were going to increase pumping, that's going to help. They did -- that remains to be seen exactly how that's going to work. That's highly variable, but it was a positive from our perspective.

Q: Okay, that's really helpful, Charlie. Thanks. And then just talking about your long-term EBITDA margin targets. Thanks for providing those, that's very helpful. You were quite a bit below that EBITDA margin range here in the first quarter despite really strong gross margin in the quarter. So, can you talk about where that leverage is going to come from in the model? Should we start to see progress towards that incrementally over the next couple of quarters as demand starts to come back? Just wondering what levers we should be kind of thinking about as you scale into those numbers?

Charles Roberson - Director, Chief Executive Officer, President and Secretary, Lakeland Industries, Inc.

The biggest element of that Alex is going to be revenue growth. We're at a point in our financial leverage, where our OpEx doesn't increase dollar-for-dollar with revenue at this point. In fact, a lot of that revenue will come with only additional expense being sales commissions. So, that's the biggest part of it. We are watching our cost. We're aware that we're at the lower end of that leverage and are being prudent with adding any to our SG&A or to those costs at this point.

Q: Okay, that's really helpful. Thank you, Charlie.

Operator

[Operator Instructions]. Okay, I'd like to turn the floor back to management for closing remarks.

Charles Roberson - Director, Chief Executive Officer, President and Secretary, Lakeland Industries, Inc.

Thank you all for joining. As I mentioned in today's call, we believe our results this quarter, in terms of both sales and profitability, will serve as a base from which we will grow the remainder of fiscal 2023.

We remain confident in our ability to deliver mid to high single-digit annual revenue growth in our core markets, gross margin levels in the low 40s, and EBITDA margin levels in the high teens to low 20s over the next three to five years. We look forward to sharing these successes with you and have a great day.

Operator

Thank you, ladies and gentlemen. This does conclude today's conference call. You may disconnect your phone lines at this time and have a wonderful day. Thank you for your participation.