Transcript of
Lakeland Industries, Inc.
Lakeland Industries Fiscal 2024 First Quarter Financial Results and Conduct Conference Call
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Participants

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Roger Shannon - Chief Financial Officer, Lakeland Industries, Inc.

Analysts

Alex Fuhrman - Craig-Hallum Capital Group

Presentation

Operator

Good day, and welcome to the Lakeland Industries Fiscal 2024 First Quarter Financial Results Conference Call. All lines have been placed on a listen-only mode. [Operator Instructions] 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 expectations for future performance that constitute forward-looking statements under federal securities laws. Any such forward-looking statements affect 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 in 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 and adjusted EBITDA. 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 - Chief Executive Officer, Lakeland Industries, Inc.

Thank you, Jenny. Good morning and thank you all for joining. I'd like to begin by pointing out that in addition to the press release yesterday, we also posted a Q1 investor deck on the Investors section of our website. And while we will not speak directly to it on this call, we do invite you to access it and follow along.

We're pleased with our fiscal first quarter results as Lakeland delivered net sales of $28.7 million, up 5.2% year-over-year. While our net sales for the quarter included $2 million from our acquisition of Eagle Technical Products this past December, Lakeland also delivered organic growth in targeted geographic markets and product lines. Of note, our fire and flame resistant arc-resistant performance product categories saw significant year-over-year growth of 103% and 55%, respectively. In terms of profitability, our first quarter gross margin of 43.4% was above our long-term target of 40% and as Roger will cover in more detail benefited from multiple dedicated actions from our team members.

In regard to our geographic markets, the North American industrial demand continues to hold strong and is performing in line with our expectations. Oil and gas turnaround activity, which was significantly curtailed during COVID is returning at a measured pace over a prolonged period partially due to ongoing labor availability constraints. We anticipate labor constraints continuing throughout the remainder of the year and are expecting an extended strong Fall turnaround season.

Going forward, we will continue to monitor global oil market developments such as the recent production cuts announced by OPEC+ and I would characterize our outlook for the year as cautiously optimistic given the shifting macroeconomic backdrop.

While our North American markets are performing in line with our targets, our Asian markets have been weaker than expected, driven almost entirely by China. China's departure from a zero tolerance COVID-19 policy in late December, significantly curtailed government demand for testing-related PPE, including disposable coveralls. Industrial economic activity has been very slow to recover as foreign customers seek to reduce dependence on China and their supply chains and as China experiences a subsequent outbreak of the XBB variant of the COVID-19 virus.

In addition to depressed industrial activity, China is experiencing post-pandemic excess inventory in its distribution channels. We anticipated an excess inventory condition would likely occur in China, but believed it would not be as severe as in the U.S. or Europe due to significantly shorter lead times within China. As a result of these factors, we anticipate China's economic recovery will remain slower than our initial projections throughout the course of the year.

Europe continues to outperform our expectations this year. But admittedly, this is because our forecast headed into the fiscal year was quite cautious given some of the macro geopolitical and energy security or supply-related issues that overhang this region. So we do not -- we do expect Europe to continue to progress this year at a pace ahead of our original expectations, even though industrial activity in general remains muted.

Turning to other important markets globally. India and Mexico are tracking slightly behind our projections for the first quarter, although we believe activity will ultimately improve and come in line with our projection for the year. Latin America is performing ahead of forecast right now and is expected to maintain this performance for the remainder of the fiscal year.

In terms of our focus on high-value products, we're seeing year-over-year success with our fire and flame-resistant arc-resistant products in North America. Our sales team has been successful in adding new distributors, expanding geographic reach and have begun displacing our competitors as key or primary suppliers with a number of existing and new distributors, resulting in 29% organic revenue growth for fire products and 55% organic growth within the FR/AR product line. Lakeland is gaining traction in these markets, and we believe that our focus on these product lines is yielding success.

Shifting gears to Eagle. Our integration efforts are tracking firmly on schedule, and we are continuing to accelerate synergy capture between organizations. This is evident in our fire business as Eagle is successfully promoting sales of NFPA-certified gear into their existing sales channels. Our legacy team is also in the process of incorporating Eagle CE Hoods into our NFPA markets and promoting Eagle CE turnout gear into our international markets. Our efforts to integrate Eagle products into Lakeland's geographic markets are initially focused on Latin America and Mexico and will be followed by India and Southeast Asia.

To this end, Lakeland's leadership team and Eagle personnel will be meeting with our Latin American and Mexico sales teams to train them on Eagle products later this month. Eagle will have a chance to learn firsthand about the South American firefighting market.

On the expansion front, we're pleased with the progress we are making at our new Monterrey, Mexico facility, which we expect to be complete by the fiscal third quarter of this year. As we have previously communicated, this manufacturing plant will greatly benefit our efforts to gain market share in higher value strategic end markets, most notably fire, flame-resistant arc-resistant high performance for electrical utilities and chemical by providing short-run capability and additional capacity to service our growing high-value product sales.

As we look to the balance of our current fiscal year, we anticipate little change in our existing business environment. We believe that China will remain weak with little in the way of economic recovery. India and Mexico were slightly behind projections as of the end of Q1 but are recoverable, and we believe they will meet revenue projections for the year. North America is currently running at forecast sales pace and is expected to continue to do so through the remainder of the year.

Europe and Latin America are both running ahead of their projections through the first quarter and do not show any signs of weakening. In the aggregate, we believe based on current market information and the strength that we are seeing in fire and industrial FR markets that we will attain our goal of mid to high single-digit growth this year.

Overall, we remain very positive on the position we are generating for ourselves within the market, and we expect to deliver continued revenue growth in our core markets as well as profitability levels in line with the company's three-year to five-year targets.

We will accomplish this through geographic targeting of specific products, turnout gear, flame-resistant arc-resistant high-performance and chemical suits, and through pricing deviations and disposables to select end user accounts where we believe we can leverage the business to capture strategic sales currently held by our competitors.

I'll now pass the call to Roger to provide an overview of our financial results. Roger?

Roger Shannon - Chief Financial Officer, Lakeland Industries, Inc.

Thanks, Charlie, and good morning, everyone. Lakeland delivered sales of $28.7 million in the first quarter. Domestic sales were $12.3 million or 43% of total revenues and international sales were $16.4 million or 57% of total revenues. This compares with domestic sales of $11.2 million or 41% of the total and international sales of $16.1 million or 59% of the total in the first quarter of fiscal 2023.

In terms of product mix for the quarter, disposables continued to decrease as a percentage of Lakeland sales and represented 43% of total revenues compared to 53% in the year-ago quarter. This again reflects the efforts we've made to shift our product mix toward higher value, higher margin and less commoditized non-disposable products as we've discussed in prior calls. Additionally, as we noted in our earnings press release issued yesterday afternoon, we saw strong growth within our fire product category, with sales up 103% year-over-year.

From a geographic standpoint, Lakeland saw strong sales growth in our U.S., Canada and European markets. However, this growth was partially offset by soft Asian sales, particularly in China and India.

Gross profit as a percentage of net sales was 43.4% for fiscal 2024 first quarter as compared to 40.5% a year ago. As Charlie already highlighted, the strong improvement in our gross margin performance was driven by deliberate sales focus on higher value products as well as improved finished goods material costs and lower manufacturing expenses. Compared to the prior quarter, our gross margin percentage increased 6 percentage points, up from 37.4% due to an improved product mix, the absence of excess freight expense write-offs that we had in Q4, profit in Q1 ending inventory and a positive Q1 inventory reserve adjustment.

Lakeland reported operating profit of $1.9 million in Q1 2024 as compared to $1.4 million in the first quarter last year. As a result, operating margins were 6.8% in the first quarter, up from 5.3% for the first quarter of last year. Our operating profit benefited from the improved gross margins and higher revenue, as previously discussed, partially offset by an increase of $900,000 in operating expenses in Q1 of 2024.

The increase in operating expenses is attributable to increases in severance expenses and currency fluctuations, travel and trade show expenses, and higher professional fees. Currency fluctuations primarily related to the Argentinian peso, which totaled approximately $300,000 negatively affected operating profit.

Lakeland delivered net income of $1.3 million or $0.18 per basic and diluted share during the quarter. This compares to $1.1 million or $0.15 per basic share and $0.14 per diluted share in the prior period.

EBITDA for the first quarter of fiscal 2024 was $2.4 million compared to $1.9 million for the first quarter of fiscal 2023. Adjusted EBITDA was $2.8 million in Q1 2024 compared to $2.3 million in Q1 of '23.

Moving to the balance sheet. Lakeland ended the quarter with cash and cash equivalents of approximately $26 million, an increase of $1.4 million compared to our fiscal year 2023 year-end cash balance of $24.6 million due primarily to cash provided by operating activities of $3.7 million for the three months ended April 30, 2023. The company continued to have no debt at the end of the quarter and has up to $25 million available from bank credit facilities.

Capital expenditures for the three months ended April 30, 2023, were $700,000 and were related to capital equipment for the company's new manufacturing facility in Monterrey, Mexico that's scheduled to open in the second half of the current year, as Charlie previously mentioned.

As a reminder, we anticipate fiscal 2024 capital expenditures to be approximately $3 billion as we complete the new manufacturing facility in Monterrey, Mexico and replace existing equipment in a normal course of operation. We expect to fund the capital expenditures from our cash flow from operations.

The company purchased $300,000 of common stock under its repurchase program during the quarter, leaving approximately $5.1 million remaining under the current authorization. Lakeland was also pleased to pay its initial quarterly dividend of $0.03 per share to stockholders during the quarter.

Our inventories declined slightly quarter-over-quarter to $58.2 million at January 31, 2023, to $57.9 million at the end of Q1 '24. Raw materials inventory increased by approximately $400,000, while finished goods inventories decreased by approximately $500,000. Our increase in raw material inventory is driven by increases in our higher value strategic products.

Moving forward, we remain committed to accelerating the reduction of our finished goods inventory this year as previously communicated and will continue to explore various price deviations on additional product styles.

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

Operator

Thank you very much. At this time we are opening the floor for questions. [Operator Instructions]. Thank you. Your first question is coming from Alex Fuhrman of Craig-Hallum Capital Group. Alex your line is live.

Q: Hey guys thanks very much for taking my question and congratulations on a really nice quarter. Would love to talk about gross margin and what we could expect to see for the rest of this year and heading into next year. It seems like you very quickly hit your longer-term profitability target. Was there a mix shift involved in getting there? So quickly, would love to just hear your broad thoughts on what we could expect to see over the next few quarters and years?

Roger Shannon - Chief Financial Officer, Lakeland Industries, Inc.

Hey, good morning, Alex. This is Roger. Thank you for the question, and thank you for the comments. We were obviously pleased with the quarter. We did see a very nice increase over Q4 as well as year-over-year. The bulk of that increase was driven by product mix, obviously, with a slight increase in revenue driving gross profit. But the mix driving gross margin, as we talked about, the focus on the higher value strategic product line within fire and FR/AR.

The other thing as you'll probably remember, compared to last quarter, particularly we had about a 200 basis point decrease or write-off and excess freight cost in Q4, and we did a comprehensive inventory costing analysis, cost roll in Q4, can clean that up from some of the higher freight costs during the COVID period.

The other thing that I mentioned in my prepared remarks, we did have a slight adjustment into positive from profit and ending inventory in inventory reserves. Of course, we'll have those every quarter. They could go either way. But this quarter, they were positive.

So longer-term, of course, over the course of the remainder of the year, we certainly are not guiding to count on those quarterly adjustments in any inventory like we just said, but that -- we are all on track for that 40% plus gross margin that we've indicated.

Charles Roberson - Chief Executive Officer, Lakeland Industries, Inc.

Alex, this is Charlie. I also like to point out the investor deck that we did for Q1 actually does contain a bridge showing the margin improvement quarter-to-quarter.

Q: Okay. That's really helpful. Thank you guys. And then you mentioned in your remarks and in release last night that you're seeing a lot of good response to the higher value products that you've been focusing more on. Obviously, that -- it sounds like that's having a positive impact on gross margin as well. Can you give us a sense of how much of your business today is what you would call those higher value products and where you see that going over the next few years?

Charles Roberson - Chief Executive Officer, Lakeland Industries, Inc.

Yes. Alex, we're already seeing a shift to that -- it's -- we look at that in more general terms. Within our product categories, we have sales, even of the same product that may -- in one case, may be strategic or higher value where another is not. We tried -- we're trying to get that message across in the press release. We talked about how we define high value. It's an end user definition, and it really goes to the amount of effort and consultation that they put into the purchasing decision.

Now having said that, disposables with the exception of cleanroom, is we just generally consider entirely commodity or not high value. And we've seen a year-over-year shift...

Roger Shannon - Chief Financial Officer, Lakeland Industries, Inc.

Full-year.

Charles Roberson - Chief Executive Officer, Lakeland Industries, Inc.

Full-year shift in our disposables, a decline of 6% that has moved largely into the fire and the FR/AR woven categories, okay? So as we move forward in future years, I expect to see that trend continue, maybe not at a 6% a year pace. But as we keep going, I think that eventually we will see our strategic items grow to where they're a 60-plus percent maybe even as high as 65% of our total revenue.

Roger Shannon - Chief Financial Officer, Lakeland Industries, Inc.

And Alex, so again, I encourage you and the listeners to kind of refer to a couple of slides we have in the Q1 investor presentation that we posted you'd see. If you look at -- as Charlie referred to, if you look at the full-year 2023 or the year that we just finished revenue, you've got 49% of that was from disposables for Q1 of 2024, that was 43%. So as Charlie mentioned, it's a $6 million decrease compared to the full-year of last year.

The chemical remains consistent at around 20%. And where we did see the pickup was in the FR/AR, and particularly the fire. So Eagle of course, contributed having the first full quarter of performance or results from Eagle, but also as we mentioned in our prepared remarks, we're seeing organic growth in fire.

Charles Roberson - Chief Executive Officer, Lakeland Industries, Inc.

Yes. And Alex, the other part of that question is in the higher value products is where we have value for product development. We've got things that are in the -- there that represent an opportunity to grow those markets as well as to take market share from our competitors.

Q: Great. That's really helpful guys. Thank you very much.

Operator

Thank you very much. While we don't appear to have any further questions in the queue. I'm now going to hand back over to the management team for any closing remarks.

Charles Roberson - Chief Executive Officer, Lakeland Industries, Inc.

Thank you, Jenny. Thank you all for joining us on today's call. We look forward to building on our momentum and sharing our successes with you this year. Thank you, and have a good day.

Operator

Thank you, everybody. 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.