

27-Oct-2022

Valmont Industries, Inc. (VMI)

Q3 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Greetings. And welcome to Valmont Industries Inc. Third Quarter 2022 Conference Call. At this time, all participants are in a listen only mode. A question and answer session will follow the formal presentation. We ask that you please limit yourself to one question and one follow up and return to the queue to ask additional questions. [Operator Instructions] Please note this conference is being recorded.

I will now turn the conference over to your host, Renee Campbell, Senior Vice President, Investor Relations and Treasurer. Ms. Campbell, you may begin.

Renee L. Campbell

Senior Vice President-Investor Relations & Treasurer, Valmont Industries, Inc.

Thank you and good morning. Welcome to Valmont Industries Third Quarter 2022 Earnings Call. With me today are Steve Kaniewski, President and Chief Executive Officer; Avner Applbaum, Executive Vice President and Chief Financial Officer; and Tim Francis, Senior Vice President and Corporate Controller. This morning, Steve will provide a brief summary of our third quarter results commenting on our market and long-term business strategy. Avner will review our financial performance and provide our outlook and indications for 2022 and preliminary indications for 2023, with closing remarks from Steve. This will be followed by Q&A.

A live webcast of the presentation will accompany today's call and is available for download from the webcast or on the Investors page at valmont.com. A replay will be available on our website later this morning. Please note

that this call is subject to our disclosure on forward-looking statements, which applies to today's discussion, is outlined on slide 2 of the presentation and will be read in full at the end of today's call.

I would now like to turn the call over to our President and Chief Executive Officer, Steve Kaniewski.

Stephen G. Kaniewski

President, Chief Executive Officer & Director, Valmont Industries, Inc.

Thank you, Renee. Good morning, everyone, and thank you for joining us. On behalf of the entire Valmont team, I would like to start today's call by offering our thoughts to those impacted by the devastation caused by Hurricane Ian last month, which impacted seven of our facilities in Florida and the Carolinas. We are saddened by the loss of life and destruction we have witnessed and wish our team members, their families and the people in the affected regions a swift recovery from this historic storm.

This storm serves as a tragic reminder as to why we speak a lot about grid hardening and grid resiliency. Utilities and other infrastructure companies have invested and continue to invest in structures that will better withstand natural catastrophes. In the case of Ian, recovery efforts were sped along by having a more resilient infrastructure in place, allowing electricity and communication services to be restored very quickly, which is helping the region return to normalcy faster.

The industry has done a tremendous job of improving the grid by considering the intensity of recent storms. However, there are still a significant amount of grid hardening yet to be done, specifically in areas susceptible to natural disasters. As an industry leader, we continue to innovate to provide better solutions, and we are proud to work with our customers globally to improve the resiliency of the grid.

Turning to slide 4 and a recap of our third quarter. Demand remains elevated across all of our end markets despite macroeconomic volatility, reflecting the ongoing investments in global infrastructure and agriculture and our customers' preferences for our products. We achieved another quarter of record sales and earnings per share, driven by strong demand and the outstanding contributions of the entire Valmont team as they live out our core values. Our businesses have focused on technology-driven solutions to help our customers operate more sustainably. I am very proud of what we were able to accomplish this quarter.

In addition to our team's flexibility and responsiveness to meet customer demand, we remain disciplined in our pricing strategy to ensure we are capturing the full value added by our distinct offerings, as well as staying ahead of inflation, specifically wage, energy and administration expenses such as healthcare and insurance. It's important to note that our approach to pricing is not to simply adjust for variations in cost, but to also lean into the value we offer through our highly engineered solutions, superior shipped complete on time, and unmatched support for our customers.

Moving to third quarter results, sales of \$1.1 billion grew 26% year-over-year, driven by a combination of sustainable pricing and mid-single digit volume growth, resulting in the eighth consecutive quarter of double-digit year-over-year sales growth. Infrastructure sales of \$778.4 million grew 23% year-over-year, with strong sales across all product lines. Investments in grid resiliency and renewable energy sources, upgrades to aging infrastructure, and ongoing 5G buildouts continue to drive broad-based market strength globally for our products and solutions. Additionally, funding from the Infrastructure Investment and Jobs Act is being deployed, and we expect the Inflation Reduction Act to be appropriated during 2023, along with other government spending initiatives across global markets. We believe these are long-term tailwinds for our businesses.

Agriculture sales of \$327.3 million grew 36% year-over-year. The combination of strong global demand for increased food production, along with widespread drought conditions is keeping farmer sentiment favorable, encouraging irrigation and technology investments. As we had expected, the impact of our typical third quarter seasonality was less pronounced this year as we successfully delivered backlog from the second quarter. Ag market fundamentals and positive farmer sentiment have also contributed to our robust project pipeline, notably in the Middle East and Africa. Severe drought conditions are persisting across many key global markets, putting pressure on crop yields and expected stock levels, keeping global commodity prices elevated.

Turning to slide 5, we have been executing on our three strategic pillars of pursuing operational excellence with ESG focus, expanding the markets we serve, and using technology to drive productive disruption across all our organization. We are seeing the benefits of our strategic approach as we build a more resilient business. As an example, we have grown our ag tech sales with attractive margins to approximately \$83 million year-to-date, an increase of 15% over last year, on track for full year sales to exceed \$100 million. Another example is our focus on high growth opportunities in end markets with favorable and global long-term demand trends. We have done this through targeted investments and organic growth and strategic acquisitions such as our recent purchase of ConcealFab in the telecommunications market.

On slide 6 is an example of our sustainable solutions and a testament to our strategy and disciplined capital allocation framework. Over the past four years, we have successfully entered and grown our solar market presence, both in infrastructure and agriculture through acquisition and investment. The acquisition of Convert Italia in 2018, later rebranded as Valmont Solar, marked our entrance into utility solar markets. Over time, we have solidified our strategic focus on distributed generation projects that offer a more attractive margin profile, less raw material risk, and faster completion than large scale utility projects.

Our key international markets of Europe, North Africa and Brazil have more pronounced barriers to entry and favorable legislation that helps drive demand. At the same time, we have been successfully expanding our presence in the US and are targeting additional growth as we move forward. Our competitive advantages of manufacturing capabilities and a global supply chain are enhanced by our deep relationship with developers and utilities. This year, we expect to nearly double our sales to approximately \$120 million and anticipate continued robust growth in 2023.

In 2020, within the agriculture segment, we acquired the majority stake in Solbras. Their services have since been integrated with our world class Valley dealer network to provide global ag solar solutions. With the Solbras investment, we became the sole global player in this underserved market, which has tremendous growth potential, allowing farmers to enjoy our scale for projects that are typically much smaller than utility or distributed generation.

Also unique, our dealer network offers unparalleled service and support in every region of the world, positioning us to be the partner of choice for a variety of applications. Whether the grower is looking to meet Scope 3 emission goals, realize tax credits and energy savings or produce alternative power generation, our Valley dealers are there to help. We expect continued strong growth in this business. Since entering the market, we are on track to exceed \$100 million in ag solar sales by the end of this year. We are very pleased with the execution and performance of both solar teams as meaningful demand of renewable energy sources is expected to continue.

In summary, we performed well during the third quarter, building on our momentum from the first half of the year. We are on track to deliver our best full year earnings per share in the history of the company. Demand for our infrastructure and agricultural products remains robust, and our team is demonstrating our core values while

providing outstanding customer service. Our focus on operational excellence is helping us to navigate external challenges, reinforcing our confidence that we are on the right path to deliver even greater value to our customers and to our shareholders in 2023 and beyond.

With that, I will now turn the call over to Avner for the third quarter financial review and updated outlook.

Avner M. Applbaum

Chief Financial Officer & Executive Vice President, Valmont Industries, Inc.

Thank you, Steve, and good morning, everyone. Turning to slide 8 and third quarter results, my comments will focus on the adjusted results as outlined in the press release and in the Reg G disclosure in the presentation appendix.

Operating income of \$114.1 million grew 42% and sales growth of 26% with operating margins increasing to 10.4%, reflecting higher volume, improved fixed cost leverage, and continued execution of our disciplined pricing strategy. Diluted earnings per share grew 36% to \$3.49, attributable to higher operating income, partially offset by a higher tax expense due to a change in the geographic mix of earnings compared to last year.

Turning to slide 9. Operating income for the infrastructure segment increased to \$93.6 million or 12.1% of sales, driven by favorable pricing and volume growth.

Moving to slide 10. Agriculture segment operating income increased to \$47.4 million or 14.6% of sales. The benefits of higher average selling prices and additional volume leverage were partially offset by higher SG&A, including incremental R&D expense for technology investments.

Turning to cash flow on slide 11. Year-to-date free cash flow of \$117 million reflects a meaningful sequential improvement driven by diligent working capital management, including a reduction in inventory. We expect full year operating cash flows to be in line with net earnings in 2022.

Turning to slide 12 for a summary of capital deployment, we continue to maintain a balanced approach to capital allocation or reinvesting in our businesses, which enables us to grow organically and inorganically while returning cash to shareholders. Third quarter capital spending was \$17 million and we returned \$22 million to shareholders through dividends and share repurchases, ending the quarter with approximately \$166 million of cash.

Moving to slide 13, the strong cash generation this quarter, allowed us to reduce total borrowing by approximately \$60 million, further strengthening our balance sheet. Total debt to adjusted EBITDA of 1.5 times remains within our desired range of 1.5 times to 2.5 times.

I would now like to review our updated 2022 outlook as shown on slide 14. We are increasing our expected sales growth due to strong third quarter results. We now expect full year 2022 net sales to grow 22% to approximately \$4.3 billion, which includes an unfavorable foreign currency impact of approximately 2%. We are also tightening the range of expected adjusted earnings per share to \$13.65 and \$14. We are confident in our outlook for the balance of the year based on the execution of our operations, our robust backlog and strong project pipeline. A reminder that project timing in many of our businesses can be hard to predict and that changes in our geographic mix of earnings may have a more pronounced impact on our effective tax rate.

Turning to slide 15. In addition to updating our 2022 outlook, we are providing preliminary indicative guidance for 2023. Building on Steve's earlier comment regarding global demand trends and maintaining our pricing discipline, we expect 2023 year-over-year sales growth of 6% to 9% and EPS growth of 11% to 15%. This assumes steady

market demand, stabilized raw material cost, inflation in line with global central bank expectation, and continued growth in R&D investments. Other assumptions are provided on the slide.

We continue to leverage our scale and global footprint to improve margins and mitigate supply chain challenges. Strong cash generation is enabling us to support our capital allocation framework, putting us on the path to achieve our long-term financial targets and drive sustainable shareholder value.

With that, I will now turn the call back over to Steve.

Stephen G. Kaniewski

President, Chief Executive Officer & Director, Valmont Industries, Inc.

Thank you, Avner. Looking at the fundamental market drivers for our segments on slide 16. The trends that have supported us over the last several quarters appear set to continue, providing future growth opportunities. We are delivering great results due to robust demand drivers and our ability to increase output to meet this demand.

While these end market drivers remain strong, we acknowledge that growing economic uncertainty is creating headwinds for certain sectors of the economy. Demand for our products is less sensitive to general economic factors. Our backlog solidifies our confidence in our revenue projections. We are investing in capabilities, technologies, and strategic capacity improvements to better enable us to deliver on our long-term goals.

Turning to slide 17, in summary, we have demonstrated an ability to grow sales through innovation and execution, bringing unique solutions to solve the complex needs of our customers. We are doing this by advancing operational excellence across our global footprint, supported by a strong and flexible financial foundation, enabling us to invest in our employees and technology. Our disciplined approach to capital allocation has served us well, and we remain committed to making strategic investments to facilitate the achievement of our long-term goals that we believe will result in greater value creation for our shareholders.

I will now turn the call back over to Renee.

Renee L. Campbell

Senior Vice President-Investor Relations & Treasurer, Valmont Industries, Inc.

Thank you, Steve. At this time, the operator will open up the call for questions.

QUESTION AND ANSWER SECTION

Operator: At this time, we will be conducting a question-and-answer session. [Operator Instructions] One moment, please, while we poll for questions. Thank you. Our first question is from Chris Moore with CJS Securities. Please proceed with your question.

Christopher Moore

Analyst, CJS Securities, Inc.

Hey. Good morning, guys. Thanks for taking a couple questions. Well, just when you think about visibility for 2023, which sub-segments are likely least impacted by further rise in interest rates or modest recession?

Stephen G. Kaniewski

President, Chief Executive Officer & Director, Valmont Industries, Inc.

Hey, Chris. This is Steve. We've been looking at – obviously across all of our end markets and the macros really across all of them are in very good shape. And to your point about interest rates, not that susceptible at this point to any kind of interest rate increases. The utility CapEx model was just announced about a month – maybe 1.5 month ago. That's in the 6% to 8% growth range. You heard the two telecom CEOs of AT&T and Verizon in the last week reaffirmed their CapEx into next year. We know agriculture is really independent of kind of all of the general recession commentary that's out there and that's moving forward.

[ph] Lighting or transportation is both in (00:19:47) the Inflation Reduction Act and the Infrastructure and Job Act (sic) [Infrastructure Investment and Jobs Act] (00:19:53). So, there's really strong drivers across all the markets and even [ph] quotings (00:19:58) with the general recession talk tends to follow GDP. The fact is that it supports a lot of our own business. And as such, with the markets being up, we should see growth there, too. So, really not that susceptible at this time to any kind of the general slowdown that's out there.

Christopher Moore

Analyst, CJS Securities, Inc.

Got it. Very helpful. And just as my follow-up, you talked about telecom CapEx being reaffirmed, telco sales were very strong, \$92.8 million in Q3. Is that – I know there's obviously big growth coming there, but is that a sustainable level or is it likely to be kind of lumpy, up and down over the next year or so?

Stephen G. Kaniewski

President, Chief Executive Officer & Director, Valmont Industries, Inc.

Historically, telecom was extremely lumpy. It would be up, it would down, it would be up, it would down. But that was when, I would say, carrier investments had other priorities. If you think of AT&T in the past putting money toward satellite and taking it from telecom, the general consensus now is that even in a recession, nobody's going to turn their phones off. They may cut cable. They may cut satellite. So, we think it'll be a smoother rollout, plus with the mandates for coverage that are out there kind of [ph] feeds (00:21:19) the impetus to move forward. Not to say that quarter-to-quarter, we won't see some ebbs and flows, but we don't anticipate any kind of a massive pullback.

Christopher Moore

Analyst, CJS Securities, Inc.

Got it. I appreciate it. I will leave it there.

Stephen G. Kaniewski

President, Chief Executive Officer & Director, Valmont Industries, Inc.

Thanks, Chris.

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Operator: Thank you. Our next question comes from Brent Thielman with D.A. Davidson. Please proceed with your question.

Brent Thielman

Analyst, D.A. Davidson & Co.

Hey. Thank you. Congrats on a strong quarter. Steve, I guess my first – Steve or Avner, I guess my first question would just be with steel prices kind of recalibrating. Where do you expect to be able to hold on to price and where do you think you're going to see some quicker pushback from customers, I guess, especially just considering the demand environment across all your product lines is pretty strong?

Q

Avner M. Applbaum

Chief Financial Officer & Executive Vice President, Valmont Industries, Inc.

Yeah. Hey, this is Avner. I'll start off. So, overall, a couple of things here. First of all, yes, we are seeing some moderation or reduction in steel and mostly HRC. But if you really look at the other part, right, we do have – we do use a lot of plate and that actually stayed very much elevated.

A

On top of that, right, we are seeing broad-based inflation across the board in many areas. Steve mentioned them earlier in the call and you add on the energy and labor, etcetera. So, we are seeing broad-based inflation and we are maintaining our price discipline. We continue to raise pricing where appropriate and really have not needed to reduce pricing, evident by our strong demand or strong backlog. So at this point, I'd say that we are holding our pricing discipline, our pricing approach and don't see any indications that we need to lower pricing.

Stephen G. Kaniewski

President, Chief Executive Officer & Director, Valmont Industries, Inc.

Yeah. And I would add, Brent, that in utility, as you know, there's already mechanisms to give back any kind of reductions or increases in raw materials. And so, that's been accounted for in our projections as we look forward. So, that's probably the biggest area that would be susceptible to it.

A

Again, market fundamentals, what they are of supply and demand, we're looking at the value that we bring in that kind of environment and making sure that just because some headline costs move, there's other costs that have not or have continued to elevate, and we'll keep a close tab on our factory outputs and hit rates and things like that.

Brent Thielman

Analyst, D.A. Davidson & Co.

Yeah. Okay. I appreciate that. And then my follow up would just be, Steve, you touched on it in your opening remarks, but maybe just your thoughts on the timing in the positive implications of the Inflation Reduction Act on your various businesses and also whether any of the infrastructure bill is beginning to have any influence on the business today.

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Stephen G. Kaniewski

President, Chief Executive Officer & Director, Valmont Industries, Inc.

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Yeah. So I'll start with the infrastructure bill. That was the earlier approved bill that came through. We said it would take at least until the end of 2022 to start really seeing anything, we are. We're quoting jobs now. Some of the appropriations have gotten through the states to work on highways and lighting areas. And so that now is really starting to, I'll say, factor in to some of the demand profile we see into next year.

With the Inflation Reduction Act, there's a lot of good favorables in there, particularly around energy. So, whether it's solar or the transmission sector, there's some real nice benefits for us. We'll see some of it start in early 2023 in terms of the solar markets because it kind of changes the project financials for the developers pretty quickly. But really for us, again, to get through appropriations and things like that, it will be later in 2023 kind of event. But it provides good tailwinds as we look at like 2024 at that point.

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

Yes. Perfect. Okay. Thanks, guys.

Operator: Thank you. Our next question is from Nathan Jones with Stifel. Please proceed with your question.

Nathan Jones*Analyst, Stifel, Nicolaus & Co., Inc.*

Good morning, everyone.

Stephen G. Kaniewski*President, Chief Executive Officer & Director, Valmont Industries, Inc.*

Good morning, Nathan.

Nathan Jones*Analyst, Stifel, Nicolaus & Co., Inc.*

We have started to see a lot of companies start to see inventory corrections from – in the channel and from their distributors. I don't imagine that that has much of an impact for you in that you don't have much inventory sitting out there that might need to be cleared. But can you just talk about any places where that might exist or doesn't exist and what kind of impact that might have for you?

Stephen G. Kaniewski*President, Chief Executive Officer & Director, Valmont Industries, Inc.*

Yeah, Nathan, the only place where we really have any inventory in the channel is in agriculture with our dealer network. And they have actually had very low inventory levels as we've gone through the summer months. So, there's no, let's say, overhang or correction there.

If you take utilities, direct to customer. If you look at telecom, there's a little bit of inventory, particularly with the Site Pro 1 components area, but not no overhang. We're trying to meet demand there. The lighting and transportation typically goes through our rep organizations and they don't carry inventory. So, I would say there's not much of an inventory kind of correction, so to speak, in the industries we serve.

Nathan Jones*Analyst, Stifel, Nicolaus & Co., Inc.*

That's what I figured. I want to talk a little bit more about pricing and the sustainability and strategic value pricing that you guys have looked at. Historically, pricing and margins has been correlated to supply and demand. And when that's tight, you've been able to generate better margins and when it's not, margins are falling. So, it is cyclical and your businesses don't tend to correlate with the business cycle and we might be early in some of those cycles.

Can you talk about any way where you think there's a difference? Obviously, supply and demand is tight now, and so you guys have a lot of pricing power. Do you think you can maintain that pricing even in the environment, which may be a few years down the track, where that balance is not as favorable here?

Stephen G. Kaniewski

President, Chief Executive Officer & Director, Valmont Industries, Inc.

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Yeah, Nathan. I would say that we had to develop a true pricing muscle. So, we're looking at it much more regularly. We have analysts that analyze it every day, every week. That's not a trait that we had in the past, and so now that's kind of embedded within the sales organizations.

I'll say also what gives us confidence to hold it is our real push on operational excellence and building a supply chain team so that we see what's coming at us with a lot more visibility than we would have in the past. There's a materials council of senior executives in Valmont that get together on a regular basis to look at everything from hot-rolled, to plate, to zinc, to copper, you name it. We look at it and we look at what our positions are and what we should do. And so that's how we believe we'll be able to maintain a lot better pricing discipline as we go out.

And I'll say lastly, from a capital allocation perspective, part of our problem in the past is overcapacity. And I think we're being much more diligent in our capacity additions to really make sure that we're not getting too far ahead of our skis, so to speak. And I think that in the markets we serve which are fairly nichey, can help keep things a lot more moderated than maybe in the past with some of the ups and downs.

Nathan Jones

Analyst, Stifel, Nicolaus & Co., Inc.

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Thanks for that. I just had one more. I wanted to talk a little bit more about that ag solar business and the history of it. I mean, getting up to \$100 million out of that is a pretty significant chunk of the agriculture business now. Can you talk about where that's been historically, I don't think you've owned that business for very long, kind of what the growth rates have been and what you think the potential growth rates a few years might be?

Stephen G. Kaniewski

President, Chief Executive Officer & Director, Valmont Industries, Inc.

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Yeah. We bought it in maybe November of 2020 and it only had a couple of million dollars, all Brazil base. And as we went through 2021, we really started to put together a team around it. We looked at where our go-to-market would really be effective, how we could do many projects on scale. And so 2021 was kind of a year to build, and it's really paid off. Sometimes it's better to be lucky. Particularly in Brazil, where they changed legislation to give retail net metering. And so that's caused a "mini gold rush" around solar there.

And I think what we saw as a market driver for us was agriculture specifically needs to be good stewards of the environment, and many of their operations as far flung as they are could go to solar with a good cost profile. We have the ability to buy at scale, to produce at scale. So when we go against a local electrical contractor, we can obviously beat them. And so, that's why it's accelerated as quickly as it has.

And we would expect kind of at least a 15% to 20% growth rate, in line kind of with the solar market. And it's pretty underserved at this point. This is the advantage of having our dealer network that can – they do the exact same thing today. They run power. They wreck things. So they have the equipment. They have the know-how and they can help them through. And then with our custom monitoring software, our customers can see what's there and how much it's producing. So, we feel very good about the growth trajectory in both the ag solar piece and the distributed energy piece.

Nathan Jones*Analyst, Stifel, Nicolaus & Co., Inc.*

Okay. Thanks very much for taking my questions.

Operator: Thank you. Our next question is from Brian Drab with William Blair. Please proceed with your question.

Brian Drab*Analyst, William Blair & Co. LLC*

Hi. Thanks first. Steve, just on that last question, ag solar, 15% to 20% longer term. But I'm just wondering, you grew the thing from \$0 million to \$100 million in basically like a year and a half. Wouldn't 15% growth in 2023 be disappointing or the very low end of what you're expecting? Could this business potentially double again in 2023?

Stephen G. Kaniewski*President, Chief Executive Officer & Director, Valmont Industries, Inc.*

It definitely has the potential to do that, Brian. We're just looking at market figures as we look out. Of course, we allocate capital looking further out. So – but, yeah, as it gets off the ground and gets rolling, you'll see. It's just the law of small numbers. We can double it pretty quickly.

Right now, it's building scale. And so that would be the only caution there is to build our sales teams or engineering teams, build up the supply chain. In Brazil, it's strong. But in other parts of the globe, we're still in the process of building that. We've delivered some projects in, say, Bulgaria and the Middle East. Those will take time to build a further team there. But it's got great fundamentals and we have a good go-to-market strategy.

Brian Drab*Analyst, William Blair & Co. LLC*

Great. Yeah. The reason I think it's an important question, of course, is just that if you're able to add another \$100 million, I mean, that accounts for a couple of points of your organic revenue growth for next year potentially from this business that has kind of popped up out of nowhere in the last year.

But I'll just ask one more question for now. You gave us guidance for revenue growth for next year. I'm wondering if you could potentially give a little more granularity in terms of what your expectation is for volume pricing. Is there any contribution from acquisitions in there or what's the expectation for FX in that expectation? Thanks.

Avner M. Applbaum*Chief Financial Officer & Executive Vice President, Valmont Industries, Inc.*

Yeah. Sure. I'll take that one. So, we will provide additional data, of course, as we go into next quarter and finish through our budget process, etcetera. But at a very high level, we should continue to expect mid-single digit growth in the volume. Pricing, we're not going to see anything nearly like we have this year. It gets more to a

normalized and historical basis. On the currency, on the FX, right now, we're seeing about a negative 1% impact and that's kind of how we roll up pretty much [indiscernible] (00:34:58). And at this point, we're not taking in any new acquisitions into those numbers.

Brian Drab

Analyst, William Blair & Co. LLC

And pricing positive just to be clear, you're assuming...

Avner M. Applbaum

Chief Financial Officer & Executive Vice President, Valmont Industries, Inc.

Pricing is positive.

Brian Drab

Analyst, William Blair & Co. LLC

Pricing is positive. Okay.

Avner M. Applbaum

Chief Financial Officer & Executive Vice President, Valmont Industries, Inc.

That is correct. Yeah.

Brian Drab

Analyst, William Blair & Co. LLC

Thank you very much.

Operator: Thank you. Our next question is from Ryan Connors with Northcoast. Please proceed with your question.

Ryan Michael Connors

Analyst, Northcoast Research Partners LLC

Hey, thanks for taking my question. You've covered a lot, so I don't really have anything new. But wanted to just clarify a couple of things from earlier. So, you talked a little bit about – Steve, when you talked about price cost a few questions back and basically that – for the orders that are already in the door, that's already baked in the cake. There's really no benefit or detriment when raw materials move. But is that really the case across the backlog? I mean, can you dive into that a little further on the backlog? Is everything in there pure escalation deflator and you're not exposed to any risk? Or is there any component of that where things can move around?

Stephen G. Kaniewski

President, Chief Executive Officer & Director, Valmont Industries, Inc.

No, there's – there are definitely areas that things can move around. On hot rolled, as an example, we can take positions, I think we can take positions. On fuel and energy, we can take positions. On plate, we can't. The markets are too thin. They have too much variation with them. And it's one of the reasons why you still see plate over \$1,500 a ton when hot rolled is around \$700 a ton. So, it's double. There, it has to be good inventory management. It has to be the right timing to bring in raw materials.

And so earlier in this year, in the first and second quarter, we were still being pinched a little because of the stubbornly high kind of plate number, where the averages were starting to drop because of hot rolled. And so we

saw some of that. Now, there's been a lot of stabilization in that raw material. And, again, we've gotten much better not worrying about literally supply. When we first tried to buy it, it was hard to even get it in the marketplace. So, we kind of overdid it a little bit. That will help us as we go into particularly the first half of next year.

But the backlog, the further it gets out is always a potential concern. But where we are at right now as compared to where we would have been a year ago, we're in just a tremendously better place when we look at that \$2 billion of backlog and kind of knowing what kind of margins we can get out of it, how we can perform with the tight labor markets, all the supply chain disruptions that have occurred, etcetera.

Ryan Michael Connors

Analyst, Northcoast Research Partners LLC

Q

Okay. That's very helpful. Thanks. And then the other one I had was on the issue of pricing in ag and irrigation in particular. I mean, ag is not a bidding market for you like it is in telecom and transmission. So, there's a bit more of a strategy and a game theory about how the different players are going to position around price. I know some early indicators coming out of the tractor type guys about what pricing looks like for next year. I mean, is it your intent to sort of be a price leader on the [audio gap] (00:38:23) and what's – just talk about your strategy. I mean, because there's a lot of uncertainty for the farmer. I mean, what is your sort of approach to pricing in such an uncertain environment as we head into the next big selling season there?

Stephen G. Kaniewski

President, Chief Executive Officer & Director, Valmont Industries, Inc.

A

Yeah. We've always been a price leader and we're looking at input costs and service levels and things you have to do to maintain that, which are very different than they were, let's say, during the last peak in 2013. In 2013, you could outsource a lot of production pretty easily. There was available supply chain. This is a much different environment. So, we will maintain very value-based kind of pricing for all that effort and to make sure we can hold that. So, I think we went out just a couple of weeks ago with a 3% price increase between now and kind of the end of the year, just looking at all the factors that are out there.

Ultimately in this environment, with net farm income projections where they are, with crop prices where they are, if you talk to anyone during harvest, they'll say they got 280 to 300 bushels of corn under irrigation and maybe 75 or 80 under dry land. So, the value proposition is very strong for them. And you get a crop, you need water to get a crop. And over time, we want to put more in. So, we're starting to bundle the Insights products from Prospera with the pivots. And so, we've launched that over the course of this quarter. So, we'll put more and more things with the pivot to bring the value part of that up and maintain price.

Ryan Michael Connors

Analyst, Northcoast Research Partners LLC

Q

Got it. Okay. Hey, thanks for your time this morning.

Stephen G. Kaniewski

President, Chief Executive Officer & Director, Valmont Industries, Inc.

A

Thanks, Ryan.

Operator: Thank you. Our next question comes from Brian Wright with ROTH Capital Partners. Please proceed with your question.

Brian Wright

Analyst, ROTH Capital Partners LLC

Q

Thanks. Good morning. Could you give us how to think about the potential impact of Hurricane Ian on the backlog for next quarter? Or maybe that's too early, but just how to you think about how that could build the backlog over the coming quarters maybe?

Stephen G. Kaniewski

President, Chief Executive Officer & Director, Valmont Industries, Inc.

A

Hello, Brian. It's a good question. So, what we typically see when there's a large natural disaster in the utility space is we have to redo kind of where the backlog is going to ship. So, you will have to create openings in the fourth quarter for some of the emergency kind of pull orders that would come in from the different utilities in Florida. And so, we have to then push some of the existing orders out into the first part of next year.

So, that's kind of the immediate whipsaw that you'll see. It really doesn't change the volume, so to speak. It just changes the kind of mix of products that may be coming through the factories. So, it's a little bit of turmoil. Then, it settles down. The utilities all look and then they really take a real assessment as to what is going to be replaced with what kind of structure, and you'll see follow up orders there.

The longer term effect is that they all now see what was done in South Florida around grid hardening and how quickly they got back up as compared to a Katrina-sized storm. And it just reinforces with the PUC, with the government leadership, and the utility leadership that they have to harden the grid. And so, it just becomes a good strong long-term demand driver.

So, there could be a little spikes in demand, but there's never like a – typically a massive spike. They had some inventory on the ground. We had inventory that they take. But it'll just be a strong year as we look at 2023 because of that.

Brian Wright

Analyst, ROTH Capital Partners LLC

Q

Great. And so, I also wanted to follow up on one more thing. With the total debt to adjusted EBITDA kind of at the low end of the range here and – just kind of how to think about that going forward in terms of M&A, especially kind of given your success in the ag solar. And not to put kind of any areas of specific interest, but just how you think about that kind of given where your capital position is and M&A activity.

Avner M. Applbaum

Chief Financial Officer & Executive Vice President, Valmont Industries, Inc.

A

This is Avner, I'll take that question. So first of all, we're really pleased with the fact that we've really been able to generate cash over the last quarter and really strengthen our balance sheet. And we have a lot of dry powder now, which we're in really good space.

Our capital allocation strategy has not changed, right? So we have a lot of opportunities internally to invest in our portfolio, in capital, in automation, etcetera. And we do have actually a very strong pipeline of acquisitions. But we are looking at the areas where we can really add – continue to add growth, like you said in some of these markets that are really strong, like we've done ConcealFab last quarter. Steve talked about the solar area.

So, we are targeting areas where we could really drive growth, synergies, and ultimately a strong ROIC. So, we're going to put that balance sheet to use. And then, of course, after that, we do return cash to shareholders through opportunistic share buybacks, which we continue, and dividends, of course.

Brian Wright*Analyst, ROTH Capital Partners LLC*

Great. Thank you so much.

Operator: Thank you. Our next question is from Jon Braatz with Kansas City Capital. Please proceed with your question.

Jonathan P. Braatz*Analyst, Kansas City Capital Associates*

Good morning, everyone. Steve, on Valmont Solar, you mentioned that – in your commentary that you're focusing on distributed energy. Is there a diminishing interest on your part in utility scale projects?

Stephen G. Kaniewski*President, Chief Executive Officer & Director, Valmont Industries, Inc.*

No. In fact, we spent the last couple of years really building up our team to handle the utility scale, particularly on the US basis. But we just want to be very disciplined about the kinds of projects that we take. When the raw material inflation occurred around steel and the modules were restricted, there were jobs out there that from a volume perspective looked very attractive but from an operating income perspective would have been a disaster for us.

So, there's enough market growth out there that we'll be able to take utility scale, but we'll do it based on kind of the right value for us and for whoever the developer or utility happens to be. So, we do have some orders in the US. But in terms of the large scale bids, you will see us from time to time take those as we believe we can make money and lock in our risk around those orders.

Jonathan P. Braatz*Analyst, Kansas City Capital Associates*

Okay. Okay. Okay. And then secondly, what is the – maybe the prospects for additional large scale irrigation projects in Africa and the Middle East? I know you've had some here recently. But going forward, how does that – how do the prospects look for additional business there?

Stephen G. Kaniewski*President, Chief Executive Officer & Director, Valmont Industries, Inc.*

Yeah. There's still a number of large projects out there, whether that is in North Africa or the Middle East. So, they are off scale to the likes of Egypt that we had earlier and so there's a number of those. And then there is a real strong pipeline when you talk about the range of \$10 million to \$40 million kind of projects that exist. And, again, it's food – driven by the same factors, food security, growing more food locally, less susceptible to currency fluctuations, all of COVID and the after effects that kind of reaffirmed countries' desires to create more stability in their markets that way. So, it's a good driver for us and good driver for the whole pivot industry frankly.

Jonathan P. Braatz*Analyst, Kansas City Capital Associates*

Okay. Thank you.

Operator: Thank you. We have reached the end of our question-and-answer session. I would now like to turn the call over to Renee Campbell for any closing remarks.

Renee L. Campbell

Senior Vice President-Investor Relations & Treasurer, Valmont Industries, Inc.

Thank you for joining us today. As mentioned, today's call will be available for playback on our website or by phone for the next seven days. And we look forward to speaking with you again next quarter.

Operator: Included in this discussion are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements are based on assumptions that management has made in light of experience in the industries in which Valmont operates, as well as management's perceptions of historical trends, current conditions, expected future developments, and other factors believed to be appropriate under the circumstances.

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