Transcript of
Astec Industries, Inc.
Second Quarter 2015 Earnings Call
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Participants
Steve Anderson – Director, Investor Relations
Benjamin Brock – President & CEO
David Silvious – Chief Financial Officer
Rick Dorris – Executive Vice President, Chief Operating Officer

Analysts
Schon Williams – BB&T Capital Markets
Joe Grabowski – Robert W. Baird
Nick Coppola – Thompson Research Group
Jason Ursaner – CJS Securities
Ted Grace – Susquehanna
William Bremer – Maxim Group
Todd Vencill – Sterne Agee
Morris Ajzenman – Griffin Securities
Brian Rafn –Morgan Dempsey Capital Management

Presentation

Operator
Greetings and welcome to the Astec Industries Second Quarter 2015 Earnings call. At this time all participants are on a listen-only mode. A brief question-and-answer session will follow the formal presentation. As a reminder, this conference is being recorded.

It is now my pleasure to introduce your host, Mr. Steve Anderson. Thank you, sir. You may begin.

Steve Anderson – Director, Investor Relations
Thank you, Adam. Good morning and welcome to the Astec Industries conference call for the Second Quarter that ended June 30, 2015. As Adam mentioned, my name is Steve Anderson and I'm the Vice President of Administration and Director of Investor Relations for the company.

Also on today's call are Benjamin Brock, our President and Chief Executive Officer; Rick Dorris, Executive Vice President and Chief Operating Officer; and David Silvious, our Chief Financial Officer. In just a moment, I'll turn the call over to David, who will summarize our financial results and then to Ben, who will review our business activity during the second quarter.

Before we begin, I'll remind you that our discussion this morning may contain forward-looking statements that relate to the future performance of the company, and these statements are intended to qualify for the safe harbor liability established by the Private Securities Litigation Reform Act. Any such statements are not guarantees of future performance and are subject to certain risks, uncertainties, and assumptions.

At this point, I'll turn the call over to David to summarize our financial results for the second quarter.

David Silvious – Chief Financial Officer
Thanks, Steve, and good morning, everyone, thanks for joining us on this call this morning. Net sales for the quarter were $268 million compared to $277.3 million in the second quarter of 2014. That is a 3.4% decrease, or a $9.3 million decrease. International sales for the second quarter of 2015 were $73.4 million compared to $92.6 million in international sales for the second quarter of 2014, a decrease of 20.7%, or $19.2 million decrease. International sales represented 27.4% of Q2 2015 sales compared to 33.4% of Q2 2014 sales. The decrease in international sales in the second quarter of 2015 compared to the same period last year occurred primarily in Russia, in Southeast Asia, in China, and in South America, and these decreases were offset by increases in international sales in Europe, in Canada, and in India.

For the quarter, international sales decreased in the infrastructure group and the aggregate mining group and slightly increased in the energy group. Domestic sales for the second quarter of 2015 were $194.6 million compared to $184.7 million the second quarter of 2014, an increase of 5.4%, or $9.9 million increase. Domestic sales represented 72.6% of Q2 2015 sales compared to 66.6% of Q2 2014 sales.

Part sales for the second quarter of 2015 were $67.4 million. That compares to $60.2 million for the second quarter of 2014. That's a 12% increase, or a $7.2 million increase. Part sales then represented 25.2% of Q2 2015 sales compared to 21.7% of Q2 2014 sales. Part sales increased in all groups for the quarter.

On a year-to-date basis, sales were $556.8 million compared to $515.9 million in the first half of 2014. That's an increase of 7.9%, or $40.9 million increase in revenues. International sales for the first half were $151.1 million compared to $155.8 million the first half of 2014, a decrease of 3%, or $4.7 million decrease. That decrease occurred primarily in Russia, in Southeast Asia, in China, and in Mexico for the first half of 2015 compared to 2014. Those decreases were offset by increases in Europe, in Canada, in Australia, and in the Middle East. International sales represented 27.1% of net sales first half 2015 compared to 30.2% of the first half 2014 sales. For the year, international sales decreased in the agg and mining and infrastructure groups and increased in the energy group. Domestic sales for the first half were $405.7 million compared to $360.1 million in the first half of 2014, an increase of $45.6 million, or a 12.7% increase. The first half, domestic sales represented 72.9% of the total sales compared to 69.8% for the same period last year.

Part sales on a year-to-date basis were $140.5 million compared to $129.4 million for the first half of last year. That's an increase of 8.6%, or $11.1 million increase. Part sales were 25.2% of total sales this year compared to 25.1% for the first half last year.

Gross profit for the quarter in dollar terms was $62.2 million, and that compared to the same amount last year, so it remained flat as far as dollar terms go; however, as a percentage of sales, gross profit increased to 23.2% of sales compared to 22.4% for the second quarter of 2014. Our absorption variance decreased about $400,000 quarter compared to quarter from $2.8 million last year to $2.4 million this year. On a year-to-date basis, the gross profit dollars were $128.3 million compared to $118.9 million last year. That's an increase of $9.4 million, or 7.9%. The gross profit percentage remained relatively flat year-over-year at 23% this year and 23.1% in the first half of 2014. Unabsorbed overhead for the year was $4.5 million in the first half of 2015 compared to $6.1 million in the first half of 2014. That is a $1.6 million positive improvement in unabsorbed overhead.

Recall that we had previously announced that the termination of operations at our Loudon facility would occur on May 31. As a result of that, we incurred approximately $1.5 million in restructuring costs, approximately half of which was accrued in the first quarter, and we discussed that in the first quarter. The rest of it that was incurred in the second quarter. Almost all of that was encountered in the gross margin line item.

SGA&E for the quarter was $43.3 million, or 16.2% of sales compared to $40.2 million or 14.5% of sales for the second quarter of 2014. That's an increase of $3.1 million, or an increase of 170 basis points as a percentage of sales. The drivers on that increase for the quarter were about a million dollars of computer and consulting expense, $800,000 payroll and related increases, research and development increases of about a million dollars, and some unexpected high incidents in our health insurance. We are a self-insured company for health insurance purchases, and so we incurred about an addition $800,000 over the same quarter last year in Q2 of this year related to health insurance.

Now, I previously called out a run rate of something slightly north of $41 million last quarter. Obviously we didn't hit that this quarter. I still believe that we can achieve something less than $43 million on a consistent run rate, but I do believe that given our research and development spend and the implementation of ERP systems that we're going through in various subsidiaries that we do need to ratchet up the run rate prediction on the SG&A to $42.5 million or somewhere in that range, give or take just a little bit. I think that is probably a more appropriate run rate to work with.

On a year-to-date basis, SGA&E was $87.1 million, or 15.6% of sales compared to $83.7 million for the first half of 2014, 16.2% of sales. That's an increase in dollar terms of $3.4 million. For the year, the same holds true as far as the drivers of the increase in SGA&E. You had computer and consulting expenses related to ERP implementations and computer system implementations of about $2.5 million, health insurance expense increases of about $2 million, payroll and related expenses of approximately $2 million, and research and development increases of about $1.3 million. Recall that in the first quarter of 2014, we had incurred about $4 million of con expo expense. Obviously we don't have that expense this year.

Operating income for the second quarter was $18.9 million. It was $21.9 million in the second quarter of 2014. That's a decrease of $3 million, or 13.7%. The first half operating income is $41.2 million compared to $35.3 million in the first half of 2014, an increase of $5.9 million, or 16.7% increase in operating income.

Interest expense was $420,000 in the second quarter of 2015, a $311,000 increase over the $109,000 we show for the second quarter of 2014, and on a year-to-date basis it's $717,000 compared to $182,000 in the first half of 2014, a $535,000 increase. The primary driver in interest expense is that we are incurring debt and borrowing money in Brazil as we have built that factory, and it is up and going since the first quarter, and we're financing that with local borrowings in Brazil.

Other income was $420,000 in the second quarter compared to $736,000 in the second quarter of 2014 and $2.4 million for the first half of 2015 compared to $1.5 million in the first half of 2014. The primary source as usual of other income is license fee income and investment income at our captive insurance company; however, the year-to-date amount for 2015 also includes key man life insurance proceeds in the first quarter of 2015 of approximately a $1.2 million.

The effective tax rate for the quarter is 37.9% compared to 35.75% in 2014 Q2, and for the year it's 37.4% compared to 34.4% for the year in 2014 at June 30. The effective tax rate for 2015 is slightly higher than our expected rate of around 36% due to some increasing state tax rates that we're incurring as well as our inability to book tax benefits for losses at certain of our foreign companies, along with certain true-ups that we had during the quarter and year-to-date periods related to various tax audits that we have in jurisdictions in which we operate. The effective rate for 2014 is lower than our traditional effective rate due to the true-up and certain tax benefits that we receive related to our basis in certain of our foreign subsidiaries, but I do expect, and neither year has the R&D credit included in the tax rate through June 30. Recall it was passed late in 2014, so I do expect the R&D credit to be passed later in 2015, and if it is, our rate for the year would be more in the 35.5% to 36% range, which is our traditional run rate on income tax effective rate.

Net income was $11.8 million in the second quarter of 2015 compared to $14.5 million in the second quarter of 2014, a $2.7 million decrease, or 18.6% decrease. That resulted in diluted earnings for the quarter of $0.51 compared to $0.63 in the second quarter of 2014, a $0.12 decrease, or 19% decrease. For the first half, net income was $26.9 million compared to $24 million in the first half of 2014, a $2.9 million increase, or 12.1% increase. That resulted in earnings of $1.16 per share in the first half of 2015 compared to $1.04 per share in the first half of 2014, a $0.12 increase, or 11.5% increase.

Our backlog at the end of June was $229.5 million compared to $264.1 million at the end of June in 2014. That's a decrease of $34.6 million, or a 13.1% decrease. Our international backlog, the international component of that backlog was $57.5 million compared to $106.7 million at June 30th last year. That's a decrease of $49.2 million, or 46%. Our domestic backlog at the end of June increased from $157.4 million last year to $172 million this year. That's an increase of $14.6 million, or a 9% increase.

Our balance sheet continues to be very strong. We have receivables of $118.2 million at June 30th compared to $119.7 million, so down slightly, down about $1.5 million year-over-year. Days outstanding remain relatively flat. They're at 40.2 this year compared to 39.1 last year. Our inventory is at $382.8 million compared to $364.1 million at June 30 of last year an increase of $18.7 million. And our turns remain flat. We were at 2.1 last year, and we are at 2.1 inventory turns this year.

We have no money owed on our domestic $100 million credit facility, and we have $16.4 million in cash and cash equivalents sitting on the balance sheet right now. Letters of credit are $11.8 million. That leaves borrowing availability on our credit facility of $88.2 million.

CapEx for the quarter was 3.8 million. CapEx for the year through the first half is $10.7 million. We previously discussed CapEx budget for the year of about $30 million; however, we believe that the rate at which we are spending on capital, we'll end up somewhere between $20 million and $25 million, which will be relative to our depreciation. Our depreciation was $5.2 million for the second quarter. It's $10.4 million for the first half. We still believe that depreciation will hold at $23.1 million for the full year of 2015.

That concludes my prepared remarks on the financials. I'll turn it back over to Steve Anderson.

Steve Anderson – Director, Investor Relations
Thank you David. Ben will now provide some comments regarding the second quarter of this year's operations. We'll turn it over to Ben now.

Ben Brock – President & CEO
Thank you, Steve. Thanks to everybody for being on the call this morning. As we mentioned in our earnings release this morning, we were disappointed with our second quarter results. We were pleased with our year-to-date earnings per share which were up 12% versus last year, however, earnings per share in the second quarter were $0.51 per share versus $0.63 per share in the second quarter of 2014, for the decrease of 19%. Our year-to-date earnings per share were $1.16 versus $1.04 last year, for an increase of 12%. Year-to-date EBITDA was $55.1 million versus $47.7 million, for an increase of 15.5%.

Our backlog at June 30 was $229.5 million, which is down 13.1% versus last year. Domestic backlog was up 9% year-over-year, and international backlog was down 46% versus last year. International backlog was down primarily due to the strengthening of the U.S. dollar and the global mining slowdown.

Regarding international sales, we are pleased to report an increase in quoting activity in our international sales groups and the addition in multiple orders since July 1 at our Astec do Brasil subsidiary for our large aggregate processing project and for two hot-mix asphalt plants. The encouraging news for us remains that as we mentioned on last quarter's call, we continue to hear from our infrastructure customers in the United States that they are experiencing good business levels, and they have backlogs of work to do, particularly on the private side.

This has been good for our infrastructure business this year with the exception of the 45 days following the latest extension of the federal highway bill in the United States which slowed the ordering of equipment. While it will take a long-term highway bill to bring sustained growth in large CapEx spending by our infrastructure group customers, we are encouraged that our customers' equipment is running at higher capacities, and we have seen a slightly stronger hot mix asphalt plant market this year versus last year.

With regards to the highway bill, we continue to stay in close contact with our elected officials in Washington DC, and we are encouraging our customers, vendors, and other industry members to do the same through our Don't Let America Dead End Effort. More info on this can be found in our Don't Let America Dead End website. The situation remains very fluid in Washington DC with the House passing a short-term extension last week in order to set up working towards funding a long-term bill by the end of this year and the Senate possibly seeing a McConnell-Boxer long-term bill being announced as early as today. Regardless of what happens over the next ten days in Washington DC, we're optimistic that there will be the long-term highway bill of some kind passed this calendar year.

As we work and wait on a long-term highway bill, we continue to pursue new business with new products in the United States, and we continue to maintain our international effort despite the challenge presented to us by the strong U.S. dollar and depressed mining industries in some of our key markets. Our lower backlog in international is a direct result of those two developments.

Updating everyone on the pellet plant that we delivered to Hazlehurst, Georgia, line one of three continues to run; line two is near the startup phase; and line three is nearly installed in full and near the testing phase. As a continuing reminder, it's a new product that we've chosen to finance, and as a result, we'll recognize the revenue for this plant as we are paid. This will have an effect on our cash and our inventory until it's paid in full. As a reminder, the order for all three lines was for $60 million.

We expected to announce the sale of a new pellet plant last quarter. Local permitting, pellet supply contracts, and customer finance on these sized projects takes a very long time for these plants and is requiring a high level of patience for us as we progress toward the next pellet plant order. We believe that we will be in position to announce a firm pellet plant order very soon. If and when we secure the order, we will announce the order to the market.

With regards to international sales overall, given the well documented challenges globally with regards to the U.S. dollar strength, global mining, and politics, particularly in Russia, we remain challenged for the moment with regards to sales internationally. We remain committed to growing our international sales over the long term, and we will continue to maintain and in some cases increase our sales and service coverage around the globe.

To that end and as a reminder, we opened our Astec do Brasil facility in Belo Horizonte on March 26 this year, and as mentioned, we are happy to report that we have secured new work for this plant and a large aggregate equipment project and two hot mix plant orders. We are already building crushers and screens in the facility for other customers, and the asphalt plants will be manufactured and delivered this year.

On the energy side, we remain challenged in our drilling and pumping equipment with regards to shipments and margins in the second quarter, and we are not immune to the current low oil prices with regards to our oil drilling and pumper business. As a reminder, as a result of the low price of oil and overcapacity at our GEFCO Loudon facility, we regretfully informed our employees at the Loudon facility earlier this year that we will be closing the facility effective at the end of May this year. As David mentioned, this closure was completed on May 31. The total cost of this event was more than we expected, at $1.5 million year-to-date; however it was still result in cost savings in this year that will outweigh the cost of closing the facility. The product lines and related inventory at Loudon have been relocated to our GEFCO Enid facility. The main product lines at Loudon were the oil drill rigs and pump trailers.

In other energy group news, we saw stable sales in heater for gas processing operations and stable sales of wood chippers and grinders. We remain optimistic on our outlook in the energy group in the long term.

Looking ahead to the third quarter of 2015 and the rest of the year, we have seen a slower backlog at the end of the second quarter; however, we are encouraged by our opportunities on pellet plants, recent hot mix asphalt plant activity, and our optimism surrounding the federal highway bill in the United States. We are confident that our third quarter 2015 will outperform our third quarter 2014 and that we'll remain ahead of our year-to-date performance last year at the end of the third quarter this year.

As mentioned in my earlier comments, from our last earnings release to now, orders have been slower during the last three months, mainly due to the strong U.S. dollar, the short-term highway bill extension, and oil prices. That's with the exception of three areas: complete hot mix asphalt plants which have been okay during this most recent selling season into this day but have also continued at like historical levels due to the highway bill uncertainty. Wood chippers and grinders have been okay and have seen growth strength across the globe. Wood pellet plant quoting activity has increased during the second quarter. We see growth opportunities in the pellet plants, large pressures for mining despite the mining industry being down, high recycled asphalt plants that will recycle up to 65%, small commercial paving equipment which continues to be strong for us, concrete production facilities, and aftermarket parts and service.

With regards to the concrete production facilities, we delivered our first large concrete production facility during the quarter from our CEI division. We see concrete plants as a growth area starting more in 2016, but we are excited to have our first new plant from CEI delivered to our customer. The plant was sold for $1.7 million.

Part sales increased in the second quarter 12% versus the second quarter 2014, and year-to-date part sales have increased by 8.6% versus last year. We remain committed to improving our part sales volume in the long term along with working to increase competitive part sales. We are continuing to work on our lean journey with regards to manufacturing and office operations, and we do continue to see results of the effort helping us to be a better company. We will also continue to focus on our gross margins.

Looking to the whole of 2015, we do remain optimistic despite our backlog level at the end of the second quarter. We expect to continue on our operational performance versus 2014. We are optimistic that our third quarter of 2015 will be improved versus last year and that our fourth quarter has the same opportunity, and again, this is despite the current state of the highway bill in Washington DC. The majority of our customers are experiencing a stable private market, and we're focused on selling existing and new products, not only in the United States, but around the globe, although as mentioned, we are facing the currency challenge at the moment internationally.

We are also focused on growing our product sales targeted at multiple energy segments, and this includes segments of biomass, oil, and gas, and they are not dependant on the highway bill. Acquisitions remain a key piece of our growth strategy, along with organic growth through new product introductions like the CEI concrete plant and targeted sales growth efforts, both in the United States and target international markets.

That ends my comments on the quarter and the year and what's in front of us. I want to thank everybody again for taking time to be on our call and for your support as we move ahead.

I'll now turn it back over to Steve Anderson.

Steve Anderson – Director, Investor Relations
Thank you, Ben. Adam, if you would, poll for questions. I know we already have some people in the queue, so we'll open that up to the analysts here just momentarily.

Operator
Your first question comes from the line of Schon Williams with BB&T Capital Markets. Please go ahead with your question.

Schon Williams – Analyst – BB&T Capital Markets
I was wondering if we could maybe zero in the agg and mining business, maybe a bit weaker than I would have expected this quarter. It's actually fairly unusual for Q2 to back up from Q1 in terms of sales, and then I wonder if you could just maybe elaborate a little bit more about what specific end markets or minerals, where are we seeing the weakness, maybe geographically, just a little bit more detail maybe to help us kind of hone in on where the weakness is coming from. And then also maybe talk a little bit about your expectations for Q3. Seasonally Q3 tends to be weaker in that segment as well, so should we expect that to kind of follow normal historical patterns? Thank you.

Ben Brock – President & CEO
Thanks, Schon. This is Ben. I think most of what we're seeing there, our larger customers on the aggregate side are doing fine. Our customers on the onsite crushing, we've had a very wet beginning to the season, and what we're seeing is a slowdown a little bit there. Their backlogs are good, they've got the work, but it's just really slowed down a little bit.

I was with a lot of customers in the last 90 days, 42 customers, and there were very few of them that had worked a complete, full week this year. One fellow in Chicago only worked one five day week this season, and that was at the end of June, so I think that's where we're seeing the slowdown there. I do think we'll see a historical third quarter slowdown, particularly since they'll be working through their backlogs, and then I think we'll see it start to pick up on the order side first week of September.

Schon Williams – Analyst – BB&T Capital Markets
Okay, thanks. And then if I could maybe just hone in on some of the big SG&A costs. It sounds like you've got some computing and consulting. Can you just give a little bit more detail? My understanding that's an ERP implementation—just maybe a kind of a status update on where we are with that project, what inning are we in, and then maybe also elaborate a little bit on some of the R&D costs. Should we expect those types of levels over the next couple of quarters? When does that turn into kind of new product introductions that we should be kind of keeping an eye out for? Thanks.

David Silvious – Chief Financial Officer
This is David, Schon. On the computer side, we are later in the game on the major ERP implementation that we're doing right now. We have them in various stages. We have one in South Africa that's very, very late in the game. It's actually implemented. You have to clean up after the game, I guess. We're doing one here in the states that we're very late in the game on, and we have one of two that are investigating what they want to do, and so that's where we are on those. We think we've incurred most of the costs on the one here in the states, the vast majority of that, so I don't expect much more costs to come through on that, certainly not to the extent that we've experienced thus far.

On the R&D, I'm sorry, Ben, you wanted to say something about computers?

Ben Brock – President & CEO
Yes, I would just say as far as what inning they're in, on the big ones, Roadtec is going through one right now, and I would say that they're in about the seventh inning stretch. They are coming along—came out of the gate pretty slow, but they've had an order system for a long time, the legacy system. They're having to change a little bit how they operate, and that's going to help them long term. They needed to do some of those changes. So, it's cost us a little more than we wanted, but at the end of the day, long run, it's going to be great for Roadtec.

Schon Williams – Analyst – BB&T Capital Markets
Would it be fair to say that you'll be complete in 2015 though?

Ben Brock – President & CEO
Yes, they'll go live in 2016. They are not drinking from a water hose; they're taking it slow because it's a dramatic change, so I don't think you'll see the numbers that you—I know we won't see the numbers we've seen so far. They're in good shape. They're doing a lot of testing.

Schon Williams – Analyst – BB&T Capital Markets
Okay, that's helpful, and then on the new products?

David Silvious – Chief Financial Officer
Yes, on the R&D side, I would expect to see expenditures continue. As Ben said, we are targeting certain markets with new products, we're developing those products over time, and that's part of our DNA, so I would expect to see that run rate continue on R&D, and that's why I've jacked up the SGA&E slightly to where we have.

Schon Williams – Analyst – BB&T Capital Markets
Okay, and would we see any of that materialize this year in terms of new product introductions?

Ben Brock – President & CEO
I think we will. For competitive purposes, I'd rather not announce those on call, but I do think we'll see some in the fourth quarter.

Operator
Thank you. Our next question comes from the line of Mig Dobre with Robert W. Baird. Please go ahead with your question.

Joe Grabowski – Analyst – Robert W. Baird
Good morning guys. This is Joe Grabowski sitting in for Mig this morning. If we could start in the energy segment, I know you touched on it a little bit, but the orders were pretty soft in the quarter. I was just wondering maybe if you could just remind us, how many of the pieces in energy are impacted by lower crude prices, and did that impact the orders in the quarter? Were there other factors?

Rick Dorris – Executive Vice President, Chief Operating Officer
Heatec and GEFCO would be the main companies impacted by the lower oil prices, mainly at GEFCO where we build oil drilling rigs and pumper trailers.

Joe Grabowski – Analyst – Robert W. Baird
Okay, and again, is that sort of why the orders were soft in the quarter, or was it kind of upside of those two businesses?

Rick Dorris – Executive Vice President, Chief Operating Officer
No, that's the main. The bulk of it was at GEFCO, we have some orders for GEFCO.

Ben Brock – President & CEO
And Joe, so you know, that's Rick Dorris, our COO, answering that question.

Joe Grabowski – Analyst – Robert W. Baird
Okay, thanks.

Ben Brock – President & CEO
The energy group is in his group.

Joe Grabowski – Analyst – Robert W. Baird
Okay. And if crude prices kind of stay around these levels, do you expect the rate of orders to continue like that?

Rick Dorris – Executive Vice President, Chief Operating Officer
Yes, I don't expect the orders on those products to improve much until oil prices start to come back up.

Joe Grabowski – Analyst – Robert W. Baird
Okay, thanks. And then maybe moving onto the highway bill, I believe the headlines I saw were that the McConnell-Boxer funding proposal that they had would kind of get them a three-year highway bill. You guys talk a lot about a long-term highway bill. Is three years long enough to provide visibility for your customers to increase their capital spending?

Ben Brock – President & CEO
Joe, this is Ben. That would be the longest bill we've had in about ten years. It would help. One of the things that I read said it was a six-year bill with three years worth of funding in it, and then moved on the rest of the funding. That would help a lot of our customers, how they feel. Like I said, I've been with a lot of customers, and they're doing better than last year, for sure, and the feelings are pretty good. Midyear asphalt association meeting was out in Colorado in the last few weeks. The general feeling there was good coming out of there. I think we had a three-year bill that helped us quite a bit.

Joe Grabowski – Analyst – Robert W. Baird
Okay. And maybe one more from me on wood pellet plants. It sounds like the second order is pretty imminent, but you also mentioned that the quoting activity was up in Q2. Could you maybe elaborate on that a little more, and would there be a chance to maybe get a third major order by yearend?

Ben Brock – President & CEO
Yes, but I don't think it'll be as big as the one that I'm talking about in the comments, but I do think there is a very good chance at a smaller plant.

Operator
Thank you. Our next question comes from the line of Nick Coppola with Thompson Research Group. Please go ahead with your question.

Nick Coppola – Analyst – Thompson Research Group
Good morning. So, looking at the year-over-year decline in backlog in both the infrastructure and aggregate & mining groups, is that decline entirely driven by international markets? I'm trying to think about how that kind of performance syncs up with flattish public funding and stronger demand for private work domestically?

David Silvious – Chief Financial Officer
Yes, it does. It ties directly to international. The decline and backlog in both of those groups was directly a result of the international backlog, and we believe as we've seen in most cases in the market, in announcements of other companies and just what we've heard from customers, the vast majority of it is tied to the currency and the decline in those markets overseas. They cannot buy the products right now at the going rates.

Nick Coppola – Analyst – Thompson Research Group
Okay, that makes sense. And then just wanted to follow up on the SGA&E question from earlier. As we head into 2016, are you expecting to get back to that $41 million type run rate, or is the kind of R&D you're talking about going to continue to trend out and maybe lead to a little bit higher number going forward.

David Silvious – Chief Financial Officer
Yes, we're working hard on SGA&E, and as we close out some of these ERP implementations and computer costs as we try to manage this healthcare a little better, as we drive down those SGA&E costs, I would like to see it, and I think our hope, the goal of the entire management team is to see it head back towards $41 million.
Will we get there? That's hard to say. A lot of these things are unpredictable, especially things like healthcare, and you get a big case or two come through during the quarter, and it can spike, but we would love to see it head south and back towards $41 million.

Nick Coppola – Analyst – Thompson Research Group
Okay, and then last question from me—

Ben Brock – President & CEO
Nick? This is Ben. I would say to add to David's comment, $41 million is our target range. Where I'd love to see it go up as if we've got a bunch of sales and we're paying more commissions, but I think we'll definitely have one or two companies come ask us in the fall about ERP2, so we may have one or two that we approve that might keep us in the $42.5 million range like David mentioned, just to give you a little more information on it.

Nick Coppola – Analyst – Thompson Research Group
Okay, certainly helpful. Okay, and then last question on part sales, up about 12% year-over-year, I guess a bright spot in the quarter there. Could you talk a little bit about where you're seeing part sales? I'm wondering how much of that is maybe driven by a break-fix type mentality or if there's anything else that I'm missing.

Ben Brock – President & CEO
Nick, this is Ben. I think there's a little bit of break-fix mentality, still especially with the two-month extension announced, but the other thing I would say is one of the things we started to measure is a percentage of our part sales that are on competitive equipment, on other makes of equipment, and we are making headway on that.

Operator
Thank you. Our next question comes from the line of Jason Ursaner with CJS Securities. Please go ahead with your question.

Jason Ursaner – Analyst – CJS Securities
You mentioned in the prepared remarks your optimism on the federal highway bill getting passed sometime this year, so I guess just the first question, with ten days left, it sounds like you're kind of under the assumption nothing gets completed by the end of July, and we're sort of differing out towards later in the year.

Ben Brock – President & CEO
Yes, Jason, this is Ben. It's such a fluid deal up there. I was in DC twice in the last 90 days. They know they need to do it. It's how to pay for it, and I think it will be interesting to see what McConnell and Boxer might announce.

I hate to use the word dysfunctional. I just don't know if they can get anything other than an extension by July 31, so that's why the comment on by the end of the year, because I do, having been out there and seen a lot of different people, I really do get the sense that there will be a highway bill by the end of the year at the latest, not to say that they don't work a magic deal the next ten days and we don't have a longer term bill, but I think it's just very fluid right now in Washington.

Jason Ursaner – Analyst – CJS Securities
Okay, and in terms of funding levels, you've talked about increased levels in the past. There are kind of two big plans being talked about. One is a more traditional, I think it's a $275 billion, six-year bill. You mentioned that there's issues of how to fund it, but is that kind of what you're talking about in terms of level versus where we are now, or do you mean something more substantial?

Ben Brock – President & CEO
I think talking to everybody, and again, the way the wind blows up there, things change, but to me, generally, the consensus is $48 billion to $53 billion per year, what they'd like to have for a bill where they've been in the $41 billion per year range, and I think it's making up the difference and defining all the—they always call it the "pay fors." I think that's what they're trying to get done. They talk about repatriation. There was one proposal when we were up there where they wanted to do an $0.11 a gallon gas tax but then a $133 write-off for people that made $75,000 a year or less. There were a lot of proposals floating around when I was up there, and that was in late June or middle of June really. So, I think

everybody wants to do it, but all the Republicans have signed off saying that they won't raise gas taxes as long as they're up there breathing, and so they're trying to figure out a way to get the money in place to fund it. I think eventually they'll get there.

Jason Ursaner – Analyst – CJS Securities
And the really big proposal though, I know the Anthony Foxx and Joe Biden are kind of championing the grow America one, and that's a bigger bill—just no political appetite for something that large?

Ben Brock – President & CEO
I'll tell you, just being up there, nobody talks about that one very much. In fact, the last trip, I didn't hear anybody talk about that, but we are on the Hill. I did go to one group meeting. There were a lot of people, so it wasn't just me, but there was one with the White House staff, and they obviously would like a bigger bill.

Jason Ursaner – Analyst – CJS Securities
And the wood pellet system, just for the Hazlehurst plant, can you remind people what the terms are for the customer loan there and just how that gets treated from an accounting perspective?

David Silvious – Chief Financial Officer
Yes, Jason. This is David. The terms on that are that it runs through June 2016, and obviously we're working closely with them on the plant, and we've got our folks down there, and they've been down there since the beginning. As the customer, Hazlehurst, is financed by their ultimate banking partners, then they'll take us out. They have to do it by June of 2016, but they will take us out, and that point is when we'll recognize the revenue. We're financing that for them. As a reminder to everyone, we're financing that for them because it is unit number one, but it's also a marketing tool for us to show other customers, and it's an impressive sight.

Jason Ursaner – Analyst – CJS Securities
Okay, and following up on the question about quoting activity, there's been a lot written recently about the utility pellet market actually slowing down a fair amount. Coal and natural gas prices are down, the conversion to biomass is a bit less economical, and the UK government just kind of retroactively changed some of their view on the carbon credits. How do you see that kind of balancing with what you're seeing here on the quoting activity since a lot of the product ends up in Europe? Is that impacting the timing on the large order at all?

Ben Brock – President & CEO
The answer on the large order is no, it does not impact it. When they announced that, their assumption is that there was a lot of those subsidies that they had in place that were helping companies outside of the UK, and they really kind of backed off on that according to our customers. But even if that was in full, it doesn't affect the ones that we're taking to right now. There is enough need for pellets in that market right that they are needing these supply contracts, so in the long term, absolutely, it would be a concern for us, but in the short term, it's not for the projects that I mentioned on the call.

Operator
Thank you. Our next question comes from the line of Ted Grace of Susquehanna. Please go ahead with your question.

Ted Grace – Analyst - Susquehanna
Ben, I wanted to come back to one of your final prepared comments when you said that there's a focus on gross margins. If we look at Astec over the last five or ten years, gross margins have been remarkably stable, kind of 22.7% with a very, very minor standard deviation. They haven't gotten better; they haven't gotten worse, but over the last five or ten years, if you were to look at US corporate profits and margins, they've increased pretty dramatically. There's been a lot written about this. You guys haven't shown that same dynamic, and so I'm just wondering whether you or Rick could talk about

really how you aim to get there. I know that GEFCO was kind of one step. Now, that's end market driven, so that is structural in some regards but also cyclical.

But in terms of the structural opportunities, you guys have to really start improving that gross margin that's really been stable but not improved at all in ten years. Can you just walk us through what that opportunity set looks like?

Ben Brock – President & CEO
It's actually a multi-department answer. One of the things that—I mean, the first place it would start is if we could get a better marketplace as far as the US dollar being strong and then you have a highway bill off and the oil business being where it is and mining being off. We've got some pretty good headwinds. Our sales guys are doing a great job. Our market shares are really holding, and actually in a lot of cases they are up, so I think if we could get more market, we'd have a little more pricing power that we really don't have where we are right now. And I think that's step one.

Step two is in manufacturing and in offices. With our lean effort, we're ranking our divisions on that. We've got a lot of different categories that they're ranked on, and it's common across all divisions. We are getting better at that. And to a certain extent, I think that's helped us maintain our growing market shares in some places as we've gotten more efficient in the shops. We've used some of that ability to price to keep the volume. So, I think if we can get more pricing power, you're going to see that come through because just—I go through all our plants. We are getting better, so I think if we can get more pricing power, we're going to be in pretty good shape coming out of it.

And then I think the last part of that is in the part sales side where you see us slowly increasing our competitive part sales and getting more percentage of our sales of parts on our equipment. That's showing up, so I think we've got a pretty good opportunity in the long run to get that up, whereas as we've, kind of like to say, been flat for quite some time. But we've been a challenging market for quite some time, and I'm pretty proud of our guys for keeping us where we are and getting the market shares up. We're in a traditional third quarter, I think, where we're going to be in a little bit of a dog fight. I think we're going to be better than we were last year in the third. Of course, we have a little competition there, but I think we're in position to get the margin up coming up here in the next few quarters.

Ted Grace – Analyst - Susquehanna
Maybe asked differently, if we were to rewind five years ago to when your sales inflected, your sales were up 35%, 40% kind of 2010 to 2015. Would you have guessed that your gross margin would have been at that level? I recognize the headwinds in energy and mining and the impact of the dollar, but just in terms of like your internal like, I guess, assessment of your margin results. I'm assuming the answer is you're below where you would have thought you'd be given that 37% improvement in sales in five years. Is that a fair way to—

Ben Brock – President & CEO
I think maybe and maybe not, because in that, there's been a lot of R&D. The first few iterations of anything that we sell are lower margin, and you take Roadtec for an example, over that time period, just about every single product they have is brand new through tier four, and that holds true through Peterson. That holds true through to our track mine and crushing and screening equipment. We have the pellet plants that we built at Astec, the concrete plants. I mean, we've had a lot of new product innovations that kind of slows down your margin. So, my answer would be we have more volume without having more gross margin, but looking back behind it with the R&D that we have done, you can kind of say well, we've done pretty good considering all the R&D we've done.

Ted Grace – Analyst - Susquehanna
Okay, fair enough. The second question was something to just run by you. A quarter ago, it sounded like the M&A prospect list was improved sequentially. Just wondering if there is any update there on how the M&A environment feels. You guys are looking at the targets.

Ben Brock – President & CEO

I would say it feels better this quarter than last quarter.

Ted Grace – Analyst - Susquehanna
So, improved sequentially 2Q versus 1Q and 1Q versus 4?

Ben Brock – President & CEO
Yes.

Ted Grace – Analyst - Susquehanna
Any characterization of big deals, small deals, in the context of what you guys typically do, multiples, U.S. versus international?

Ben Brock – President & CEO
Well, you know, I would say I don't have an answer to that, other than yes to all of them. We have some bigger ones and some smaller ones and multiple-wise, we're not going to get too far out of the range we've done in the past.

Operator
Thank you. Our next question comes from the line of William Bremer with Maxim Group. Please go ahead with your question.

William Bremer – Maxim Group
You know, taking a positive from this quarter, I was quite impressed with the gross margins, specifically in the infrastructure and the aggregates. And my question is what you are booking now, is it at those margins or better? How do I look at pricing specifically in those two segments?

Ben Brock – President & CEO
I would say that we are booking about the same level right now.

William Bremer – Maxim Group
Okay, so, it's really about utilization that's affecting the operating income right now, but the selling price is solid?

Ben Brock – President & CEO
I would say that yes, we're okay in the selling price. I think we could do better with a stronger market.

Operator
Thank you. Our next question comes from the line of Todd Vencil with Sterne Agee. Please go ahead with your question.

Tod Vencill – Analyst – Sterne Agee
You guys mentioned, there's been a lot of talk about the federal highway bill, and rightly so. You guys mentioned in the press release, you've seen the evidence of highway projects to their own new funding mechanisms start to show up in the form of new project proposals. Can you talk about that—talk about what some of those state funding mechanisms are, where they're showing up, what kind of impact they're having?

Ben Brock – President & CEO
Sure, Todd. This is Ben. In South Dakota, there was gas tax increase. It was about, I think it was $0.10 a gallon. Pennsylvania has done funding increases through their taxes. Virginia went to a sales tax setup, so that's a few of the examples, and we've just seen our customers having more work in those areas now as a result.

Came out of the gate slow in Virginia. The economy wasn't doing as well, and then it kind of came back, so now things are a little better there. But you know strong states, I mean, there are several strong states right now. I was with a customer yesterday from Kentucky, and they've got pretty good levels of work right now, so there's good activity for our customers right now.

Tod Vencill – Analyst – Sterne Agee
So, first of all, for the state of Virginia, let me apologize for being slow about that. But beyond that, I mean, at what point can these sort of state initiatives and states taking their destiny in their own hands really make up for the fact for your customers of a lack of federal visibility, or can it at all?

Ben Brock – President & CEO
Todd, I think we're probably a couple of highway bill cycles away from something like that, where the state bills take over for the federal funds. The private side is helping them too, so there are two sides of that equation. We have about 50% of the hot mix coming from the private side work on average—now, this is in an average year—and then 50% coming from government, and you're just talking hot mix tons there. That's just a rule of thumb. Sometimes that is true or not, but that's kind of rule of thumb. But the government work represents 90% of the hope still today, because if it's a three-, four-, five-, six-year bill, that just gives them the comfort level to go with the large capex expenditure like an asphalt plant or a big crushing plant.

Tod Vencill – Analyst – Sterne Agee
That does make sense.

Ben Brock – President & CEO
I just don't see the states taking over to the level that the federal coverage would provide them. If they had a good federal bill, that would give them the mental feeling and the coverage to pull the trigger on the big projects.

Tod Vencill – Analyst – Sterne Agee
All right, that's useful. Thanks. And then switching gears to just the financial side, obviously stronger dollar as well as sort of weaker international mining conditions are going to impact your results, but to what extent did just straight translation hurt you in the quarter, if at all, of foreign currency to dollars?

David Silvious – Chief Financial Officer
Yes, and we did that measure, and for the quarter, it's about $4.5 million on the revenue line.

Tod Vencill – Analyst – Sterne Agee
Okay. Do you have a similar number for the backlog?

David Silvious – Chief Financial Officer
For the backlog, it hurt us about $4 million as well.

Tod Vencill – Analyst – Sterne Agee
Got it. Thank you for that. And just, you may have mentioned this, but just to sort of frame it up, you talked about the lean journey for a while. I know that's a big part of a lot of things you guys are trying to do. Where do you feel like you stand on that, and where does that go from here?

Ben Brock – President & CEO
Remembering that we were slow to that, the last few years is when we really started to focus on it. If a score of 100, it would be the end of the journey, which I don't know if you're ever at the end of the lean journey based on where we are today. But if the 100 was that, I still think we're not—I don't know, I would guess halfway to 60%. I mean, we have a lot still that we can do to improve our factories and our office operations. It's just not in the factory. That's a gut feel from being in the plants and talking with our guys and looking at our rankings and the things that we're working on.

Tod Vencill – Analyst – Sterne Agee
All else equal, if you were at a 100 today, you think you'd be at 25% gross margins or higher or lower?

Ben Brock – President & CEO
I think we'd be in the 25% plus range.

Operator
Thank you. Our next question comes from the line of Morris Ajzenman with Griffin Securities. Please go ahead with your question.

Morriss Ajzenman – Analyst – Griffin Securities
Can you run through your groups and just give us examples where you feel you have either lost market share or gained market share in any one category over the past handful of years again?

Ben Brock – President & CEO
Morris, this is Ben. We have over 220 product lines, but by group, I would tell you that we have in the most cases held onto market share and a few cases we have gained market share, and where we have slight market share loss would be probably in the highway pavers but not by much. But we haven't really lost a lot, and part of that is there has been a lot of rent to own in the last selling season. But again, Roadtec's doing pretty well through the first half, so it's hard to get too critical on Roadtec on that. But if there was one place where I would say we had lost any, and it wouldn't be much, that would probably be where it is. Everywhere else, we've done a fine job holding onto market share.

Operator
Thank you. Our next question comes from the line of Brian Rafn with Morgan Dempsey Capital Management. Please go ahead with your questions.

Brian Rafn – Analyst – Morgan Dempsey Capital Managment
Let me ask you a question for Ben. We've been beating this highway bill to death, and I'll beat it a little more. If you follow the ASCE, the Society of Civil Engineers' infrastructure report cards, I think the last one was 2013, I've been watching them for decades, and I actually see some categories now in infrastructure that are rated F, and when you go up to Washington, Ben, do you get a sense of that they understand the gravity? We used to be able to put guys into space and build Navy ships, and now we can't even pass budgets.

Ben Brock – President & CEO
It's frustrating, walking around up there, to be honest. I would say that there are those that get it and understand it, but sometimes you try to hold your patience. One of the meetings, I shouldn't say what I said to him, but I just said it's easy to sit here in DC where you fix the roads for the tourists, and I know what district they were from and how good the contractor was in their district. And I said it's easy to fly back and forth in between those areas where you have great contractor and great roads and then back to DC, I said, but I've been to 16 states in the first half of the year, and I could tell you it's falling apart. I just don't know that they get that.

Now, I do think that the majority of them understand they need to do something. I do think they've gotten the messages. I think our associations have done a great job of giving them those stats, Brian, I really do. I think most of them get it. That was a one-off, and I'm sorry, I was emotional about that, but I do think they know they need to do it.

Brian Rafn – Analyst – Morgan Dempsey Capital Managment
Okay, all right, fair enough. You talked a little bit about some of the regionals. Here is Wisconsin, we've rebuilt four interchanges out of Milwaukee. You can't drive five miles once you hit a detour sign.

There are some states like Texas, Wisconsin, Indiana, that through private-public partnerships and that have had some pretty strong state DOT activity, and I'm wondering if the gas tax stuff that you talked about in Virginia, Pennsylvania, South Dakota lately, have you seen regional strength with road builders buying from states over the past few years that may have had stronger state DOT funding than, say, other states?

Ben Brock – President & CEO
Yes, I would say that Texas would be one of those states. Florida would be one of those states. Oklahoma has been okay for some of our customers, so those would be the ones that would come to mind just talking here on the phone.

Brian Rafn – Analyst – Morgan Dempsey Capital Managment
Okay. Okay. You talked a little bit about kind of the wood pellet plants. When you're looking at down the road, two, three, four years, exploratory conversations, potential quoting, how many customers, would you be having dozens on conversations? What's kind of the scale of the level of interest being new venture for you guys?

Ben Brock – President & CEO
At this point, I would say it is not dozens, but dozen, 12 to 15 right now.

Brian Rafn – Analyst – Morgan Dempsey Capital Managment
Okay, all right. Let me ask, if you looked across all of your subsidiaries, what would you get a sense of kind of your capacity utilization rates, and if and when, and it will turn, things will turn around where you go from absorption issues to issues of overtime, and you don't have enough, what might be your rough line sales revenue capacity with all the operating assets you have deployed today?

Ben Brock – President & CEO
It depends of where that business comes into Brian, by division, but I would say probably in the $1.5 billion to $1.7 billion range. We could handle a lot of work up to that. That being said, I'd tell you our utilization would sound better than that right now, but we're not working three shifts in every place, so maybe we could add shifts and add people. Our ability to get people is fairly good in most locations. We have some where the unemployment is still really low, but by and large I think we could get good people to be able to go up in the 1.5 range pretty quickly.

Brian Rafn – Analyst – Morgan Dempsey Capital Managment
Yes, okay. Let's go to worst case scenario and say that we stumbled through, and we don't get a highway bill this year. At what point do you see either with the big national road builders or the regionals, where you're seeing things just break down, and at some point they're going to have to start looking at actually making some purchases, or do you not see the purchases and it just shows up in more increasing and accelerating part sales?

Ben Brock – President & CEO
Brian, I think we might have seen a little bit of that through the buying season this year, because it was a little more, just a little more stable. It wasn't much, but it feels a little more stable. There are people still looking on the plant side right now. So, I would think we might be seeing that on a small scale right now, because the plants have been running a little more in the last year, so I think we may be seeing that just a little bit. I don't know that that wouldn't be at the end of the '16, '17 type buying season event more than a this year event.

Brian Rafn – Analyst – Morgan Dempsey Capital Managment
Yes, okay. And then final, if you look across the entire Astec company, where is your ERP system roll-off? Do you still have other subsidiaries that still are yet to install that, or is it finished within the next couple of years?

Ben Brock – President & CEO
The larger divisions by and large are pretty close to all having new systems that will be good for a decade or more, and then some of the smaller divisions may do them, but they'll be much smaller in price too, because there's less users. So,

we're also having everybody choose one of two systems, so we're getting more continuity across the board, and we're getting better at putting them in. That helps us. We're doing more, best practices sharing, so I think we're going to be seeing that come down probably after next year pretty significantly.

Brian Rafn – Analyst – Morgan Dempsey Capital Managment
Okay, and then on the energy side, the oil rig construction or the pumper trucks, how much surplus equipment, used equipment, is floating around where you'd have to see a sustained increase for months or quarters or years relative to holding spot prices higher in oil and gas, or would you see that kind of recover fairly quickly?

Rick Dorris – Executive Vice President, Chief Operating Officer
This is Rick Dorris. There is defiantly some surplus equipment available right now, rigs and pumpers. It would probably take several months of sustained increases in the prices to try to use up some of that inventory, but after that, I think we'd have good change of selling some new equipment in those areas.

Operator
Thank you. Ladies and gentlemen, there are no further questions at this time. I would like to turn the floor back over to management for closing comments.

Steve Anderson – Director, Investor Relations
Thank you, Adam. We appreciate everyone's participation on our second quarter conference call. Thank you for your interest in Astec.

As our news release indicates, today's conference call has been recorded. A replay of the conference call will be able through August 4, 2015, and an archived webcast will be available for 90 days. A transcript will be available under the Investor Relations section of the Astec Industries' website within the next seven days. All of that information is contained in the news release that was sent out earlier today.

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