Management's Prepared Remarks
Third Quarter 2024 Earnings Conference Call
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PI Aquino
Vice President, Investor Relations

Good morning and thank you for joining us today. I'm joined by Robert Buck, our President and Chief Executive Officer, and Rob Kuhns, our Chief Financial Officer.

We have posted our earnings release, senior management's formal remarks and a presentation that summarizes our comments on our website at topbuild.com.

Many of our remarks today will include forward-looking statements which are subject to known and unknown risks and uncertainties, including those set forth in this morning's press release and in the Company's SEC filings. The Company assumes no obligation to update any forward-looking statements because of new information, future events, or otherwise.

Please note that some of the financial measures to be discussed during this call will be on a non-GAAP basis. These non-GAAP measures are not intended to be considered in isolation or as a substitute for results prepared in accordance with GAAP. We have provided a reconciliation of these financial measures to the most comparable GAAP measures in today's press release and in our presentation, both of which are available on our website.

I'd like to now turn the call over to our President and CEO, Robert Buck.

Robert Buck
President and Chief Executive Officer

Good morning and thank you for joining us today. We're proud to share that in the third quarter, we reached another historic high for TopBuild's sales and adjusted EBITDA performance. Our teams did a very good job across both our Installation and Specialty Distribution segments, posting top-line growth and bottom-line profit expansion. This quarter is a prime example of our ability to perform well in any environment.

The landscape for building products in the third quarter was, in many ways, much like the second quarter. Although we've seen improvement in inflation metrics and the labor market is strong, housing demand in the second half of the year has been slower than anticipated.

Single-family residential starts still vary widely across the country. Even as mortgage rates drifted lower ahead of the Fed rate cut in September, homebuyer behavior suggests that consumers are holding out for a lower rate environment and election certainty. More recently, mortgage rates have been on the rise again.

On the multi-family side, we are still working through our backlog. Multi-family demand has slowed and we are not expecting it to improve in the fourth quarter and as we move into 2025. As a reminder, multi-family units typically require about 40% of the insulation when compared to a single-family unit, and our business is much more weighted toward single-family, consistent with the industry.

On the commercial and industrial side, bidding is still very active, and we have a strong backlog going into 2025. As we talked about last quarter, some project starts have been pushed out, primarily for financing reasons. We have not seen an uptick in cancellations, so we anticipate that when the financing environment improves, these projects will move forward.

Turning to our results, we performed very well in the third quarter given the macro environment. Sales increased 3.6% to $1.37 billion as we grew volumes, benefited from acquisitions and realized pricing across both Installation and Specialty Distribution.

Our adjusted EBITDA totaled $285.1 million, and adjusted EBITDA margin was 20.8%.

Moving on to our operations, with over 14,000 employees, we are a people business, and everyone plays a key role in what we achieve every day. We continue to be pleased with our ability to attract labor, align incentives and develop and reward our employees accordingly.

On the material side, fiberglass is still on allocation. Planned and unplanned maintenance remains persistent with the manufacturers and the new manufacturing facility in Texas has been slower than anticipated coming on-line. Our teams are doing a good job managing in the continued tight supply environment.

Our Special Ops team continues to be an important part of our story and how we continue to improve productivity and drive profitability, as you see in our results.

As I have done in recent calls, I want to spend time highlighting a particular area of our business to provide a better understanding of our differentiated model.

Today I want to briefly touch on Crossroads, our Canadian specialty distribution business in mechanical and metal building insulation. Crossroads joined TopBuild through the acquisition of Distribution International in 2021. With its long history in Canada, they're a leader in the commercial, marine and industrial end markets.

We operate out of 18 facilities located in key markets across Canada, and our focus is to deliver the best service possible for our customers. Our value-added specialty fabrication capabilities differentiate us from the competition and enable us to be the go-to supplier of innovative products and resources for our customers.

Our focus includes both the ongoing maintenance of commercial and industrial facilities and a diverse and impressive list of new construction projects.

One of our more notable projects for which we are currently the lead supplier is a liquefied natural gas project on the west coast of British Columbia. This is the largest infrastructure project in Canada's history.

We are also the lead supplier for a large shipbuilding program for the Canadian Coast Guard, as well as numerous nuclear power and oil sands projects.

Our Crossroads management team is highly accomplished and we're very proud of their hard work. They've been driving the business forward and have consistently achieved growth above the market.

Turning to capital allocation, M&A is a core competency of TopBuild, and acquisitions continue to be our number one capital allocation priority. We have a solid track record of generating strong returns for shareholders.

We are pleased to have recently announced the agreement to acquire Shannon Global Energy Solutions, a mechanical insulation company serving multinational commercial and industrial customers. Shannon is based in upstate New York and generates approximately $11 million in annual revenue. This brings our 2024 year-to-date acquisition count to 7 for a total of approximately $118 million in annual revenue.

Given our robust pipeline and very active M&A environment, we are allocating more resources to support our M&A efforts as we evaluate several opportunities across our end markets.

We continue to concentrate on our core of insulation and we are also learning about opportunities that have the potential to expand our total addressable market. Importantly, we will stay disciplined as we focus on those opportunities that best leverage our core competencies.

Also in the third quarter, we continued our share buyback program, repurchasing 1.07 million shares for a total of $413.9 million.

As you saw in our press release this morning, and considering today's macro environment, we are tightening our outlook on 2024, which Rob will cover in more detail.

Before I turn it over to Rob, let me reiterate that we are performing very well in a macro demand environment that has been choppier than anyone anticipated at the beginning of the year. Despite this, 2024 will be another strong year of profitable growth for TopBuild. We are very well positioned to capitalize on improving demand that we believe will materialize as 2025 progresses.

We participate in a great category and industry, and we have a differentiated business model. The underlying fundamentals are strong – an underbuilt housing market in the U.S., rising household formations, and the prospect for lower interest rates.

These factors, coupled with the critical role that insulation plays in driving energy efficiency and meeting strengthening building codes, demonstrate why we're bullish about the long-term growth opportunity for TopBuild.

Rob Kuhns
Chief Financial Officer

Thanks Robert. I'd like to extend my thanks to our teams for their hard work in delivering another excellent quarter.

As Robert noted, record high sales of $1.37 billion grew 3.6% versus prior year, with both segments showing growth year-over-year and sequentially. M&A, net of a disposition, contributed 2.3%, while price was up 1.0% and volume improved 0.4%.

Third quarter pricing of 1.0% reflects the continued realization of higher fiberglass pricing net of new price reductions on spray foam driven by increased supply.

Turning to our segments, Installation sales grew 4.2% to $856.4 million. Net M&A added 2.7%, pricing contributed 1.1% and volume was up 0.5%.

- Residential sales improved slightly from the second quarter and grew 3.7% vs. prior year due to M&A and single-family growth, partially offset by slowing multi-family sales.

- Commercial sales also improved slightly from the second quarter and grew 6.8% vs. prior year due to M&A and timing of projects.

Specialty Distribution sales rose 5.1% to $600.4 million in the third quarter. Volume improved 3.0%, acquisitions added 1.4%, and pricing contributed 0.8%.

- Sales to the residential end market improved slightly from the second quarter and grew by 8.5% vs. prior year.

- Sales to the commercial and industrial end markets slowed slightly from the second quarter and grew by 2.9% vs. prior year.

Third quarter adjusted gross profit of $421.8 million, or a 30.7% margin, was 100 basis points lower than last year. As we've discussed in the past – our 2023 third quarter results included a one-time benefit of approximately $15 million from higher-than-normal margins on multi-family and commercial projects in the Installation segment.

Excluding this, adjusted gross margin improved by 10 basis points versus last year, as we continue to focus on driving productivity and profitability across our operations.

Third quarter adjusted SG&A as a percent of sales was 12.8%, an improvement of 40-basis points versus last year.

TopBuild adjusted EBITDA in the second quarter totaled $285.1 million, or a margin of 20.8%. Excluding the $15M margin benefit from last year, we expanded adjusted EBITDA margin by 50 basis points.

- Installation segment adjusted EBITDA margin was 22.3%, a 40-basis point improvement after excluding last year's $15 million benefit.

- Adjusted EBITDA margin for the Specialty Distribution segment expanded by 20 basis points versus 2023 to 18.4%.

Other income and expense of $16.1 million in the third quarter was $3.3 million higher than prior year due to lower interest income which was driven by lower cash balances.

Third quarter adjusted earnings per diluted share of $5.68 improved 4.6% compared to last year.

Moving to our balance sheet and cash flow, total liquidity was $693.6 million at the end of the quarter. Cash was $257.3 million, and we have $436.2 million of availability under our revolver.

We ended the quarter with net debt of $1.14 billion, and our net debt leverage ratio was 1.06 times trailing 12 months adjusted EBITDA.

Working capital as a percentage of sales was 14.1%, an improvement of 50 basis points compared to the prior year.

Free cash flow for the trailing 12 months totaled $698.0 million, representing a 2.6% improvement over the same prior year period.

We continue to strategically allocate these strong free cash flows, and our capital allocation priorities remain unchanged, with acquisitions our top priority. This year, we have announced 7 transactions, and we continue to have a very healthy pipeline.

Our second priority remains returning capital to shareholders and in the third quarter we bought back $413.9 million or 1.07 million shares. That brings our year-to-date share buybacks to $919.2 million or 2.3 million shares. As of September 30, $235.2 million remains under our current share repurchase authorization.

Finally, turning to our outlook, we are narrowing our full year guidance.

- We expect to finish the year with sales between $5.3 and $5.35 billion, which represents year-over-year growth of 2.5% at the midpoint.
- We have also tightened our adjusted EBITDA expectations to $1.055 to $1.085 billion.

While the macro environment has not played out the way we originally thought this year, 2024 is shaping up to be our 9th consecutive year of sales and profit growth, something we are very proud of.

While the choppiness of our end markets is likely to continue into the first half of 2025, we think the underlying fundamentals for demand in our industry remain strong, and we are confident that we will continue to drive profitable growth and increase shareholder value.

Robert Buck
President and Chief Executive Officer

Before opening the call up to questions, let me reiterate some of my opening remarks.

- We have a proven, differentiated business model, a disciplined capital allocation approach and an ongoing focus on strong execution and driving improvements throughout the business.
- As we look ahead, the macro fundamentals of our business are supportive of construction demand growth. We are inherently well positioned to capitalize on the opportunities for increased energy efficiency and strengthening building codes.
- We continue to have a significant opportunity to drive growth through M&A. Our pipeline is healthy, and we are very active. We have a great track record of evaluating, acquiring and integrating businesses, generating solid returns.
- We remain committed to building on our track record of delivering increased shareholder value and we expect 2024 to be another strong year of profitable growth.

I'll conclude by thanking our teams for their continued dedication, focus on our customers and commitment to safety. We want to thank you for your efforts to consistently execute and drive improvement across our business.

With that, operator, we are ready to open the line up for questions.