

**Titan International, Inc. (TWI)**  
**Transcript of Q3 2020 Earnings Call and Webcast**  
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***Company Participants***

*Todd Shoot - Senior Vice President, Investor Relations and Treasurer*

*Paul Reitz - President and Chief Executive Officer*

*David Martin - Senior Vice President and Chief Financial Officer*

***Conference Call Participants***

*Joseph Mondillo - Sidoti & Company*

*Komal Patel - Goldman Sachs*

*Kirk Ludtke - Imperial Capital*

*Justine Ho - Mesiroow Financial*

**Presentation**

**Operator:** Good morning, ladies and gentlemen, and welcome to the Titan International Inc. Third Quarter 2020 Earnings Conference Call. (Operator Instructions) It is now my pleasure to turn the floor over to Todd Shoot, Senior Vice President, Investor Relations and Treasurer for Titan. Mr. Shoot, the floor is yours.

**Todd Shoot:** Thank you, Debbie. Good morning, and welcome, everyone, to our third quarter 2020 earnings call. On the call with me today, we have Titan's President and CEO, Paul Reitz; and David Martin, Senior Vice President and CFO. I will begin with the reminder that the results we are about to review were presented in the earnings release issued this morning, along with our Form 10-Q, which was also filed with the Securities and Exchange Commission this morning.

As a reminder, during this call, we will be discussing certain forward-looking information, including the company's plans and projections for the future that involve risks, uncertainties and assumptions that could cause our actual results to differ materially from the forward-looking information. Additional information concerning factors that either individually or in the aggregate could cause actual results to differ materially from these forward-looking statements can be found in the safe harbor statement included in today's earnings release attached to the company's Form 8-K filed earlier today, as well as, our latest Form 10-K and Forms 10-Q, all of which have been filed with the Securities and Exchange Commission.

In addition, today's remarks may refer to non-GAAP financial measures, which are intended to supplement but not be a substitute for the most directly comparable GAAP measures. The earnings

release, which accompanies today's call contains financial and other quantitative information to be discussed today as well as a reconciliation of the non-GAAP measures to the most comparable GAAP measures. Today's earnings release is available on the company's website within the Investor Relations section under News & Events. Please note, today's call is being recorded. A copy of today's call transcript will be made available on our website. I would now like to turn the call over to Paul.

**Paul Reitz:** Thank you, Todd. Titan has done a good job again this quarter navigating through the uncertainty and challenges of the pandemic to report another period of solid financial results. We continued on what we achieved in the second quarter with stronger margin performance, good working capital management and improvements to our balance sheet.

Diving into the business, I believe we had a really good quarter on nearly all facets of our business that are within our full control. We did see a top line decrease of nearly 12% when compared to last year as some of our end markets continue to be heavily influenced by the COVID pandemic, along with about half of that decrease coming from the impact of negative currency fluctuations.

However, despite this decline in sales, we were able to deliver a 250 basis point increase in our gross margin percentage to 10.3%. Also as we've seen throughout this year, we have been and we will remain diligent in managing our controllable costs. This period, excluding the \$5 million Geico legal accrual, we were able to reduce SG&A by over 12%.

The positive actions by the Titan team throughout all of our businesses resulted in adjusted EBITDA of \$14.2 million, which is an increase over last year's third quarter and this year's second quarter as well. Perhaps most importantly for Titan was the continuing progress we made with our balance sheet as we increased our cash by \$18 million from last quarter and continue to lower our debt.

In fact, our net debt represents the lowest level we've had since Q3 2018 and has improved or has been reduced, I should say, by over \$85 million over the past 12 months. Our third quarter results demonstrate our solid operational and financial execution in dealing with COVID and obviously, the many business-related channels that go along with that.

We now anticipate our full year adjusted EBITDA to exceed 2019 levels and be in the range of \$40 million to \$44 million, assuming no further unexpected COVID-related shutdowns.

On that COVID front, we all are experiencing the daily barrage of news, which has tilted negative in recent days with the concerns over a second wave that has resulted in additional lockdown measures in

parts of Europe and here in the U.S. with increased hospitalization. There is clearly global business risk associated with this concerning trend that can't be overlooked. However, looking specifically at Titan's end markets, we definitely feel there are reasons to be positive as we look towards the near future.

So starting right here in North America. Over the past couple of months, we've seen positive trends in North America AG as conditions have continually been on the upswing. We noted -- we know the last quarter that we are seeing more drop in orders, but that momentum has grown stronger as we now see more firm orders as corn has also been hovering in that \$4 range and soybeans have reached multiyear highs. Throw on top of that, \$14 billion in direct government payments going to farmers prior to year-end, all this leads to net farm income around \$103 billion, which is an increase over 20% from last year.

Farmers sentiment levels are reflecting this as they are now reaching a 5-year high. And in addition, there have been solid improvements in the dealer sentiment with 30% of AG dealers now reporting current inventory levels are too low. This is the first time this has occurred since mid-2012, and so it's reversing a trend of too much reported inventory for the past 8 years.

Forest farmers are not going to run out and start freeing with the money just cause corn is at \$4, but there is really good momentum that should be kick-started in the replacement cycle. For example, we started to see that in some recent information where 42% of AG dealers already see their sales going up by at least 2% in 2021, with close to 10% of the dealers expecting sales to increase over 8%. Keep in mind, 2020 actual sales levels have exceeded the initial dealer forecast at the start of this year.

Moving down to Latin America. I've spoken extensively for good reason about the strong business improvements that have been made in Titan Brazil through the years. Unfortunately, financially speaking, they've been somewhat hit in our results by the continuous weakening of the Reais. Nonetheless, we have made extensive investments in recent years to significantly improve our capacity in key product sizes. And just in the past 2 years, we have developed over 60 new products.

These actions have paid off well already with increased sales and increased gains in market share as well. But as we enter 2021 with demand at really high levels already, the prior investments position Titan Brazil extremely well for the near future.

So sliding away from AG over to earthmoving and construction, clearly, the segment remains challenged. We saw our sales slid -- slide 19% this quarter. As I said earlier, though, we've done a good

job of managing margins. It's evident in this sector as well, where we were able to push up our margin 180 basis points to over 10% from 8.3% last year.

While these market conditions currently remain on the tougher side, there are market signals that are starting to bode well for next year, as dealer inventories are low, global housing continues to show growth. Plus, we already have Europe on leasing and infrastructure spending bill, obviously, use it as a mechanism of a rebound from the pandemic, but that's going to put pressure on other governments to feel that they need to do the same as well.

Our ITM business, on top of all the changes that are going on in the world that are being induced by the pandemic, our ITM business is well positioned geographically to benefit from the regionalization of supply chain, which will be a continuing trend. Despite these market conditions, in recent months, our ITM business has also been solidly beating our internal forecast as order patterns have consistently improved. With that being said, we do see 2021 as being a rebound year for our undercarriage business, perhaps not as much in the first half, but by the second half, market conditions should demonstrate really good signs of life.

We aren't just going to sit back and ride the market condition improvements to increase our sales. We do expect our efforts in product development within North and South America tire businesses, along with what we've done to develop new products in our undercarriage business to drive a fair amount of new business in 2021. You put all these pieces together and it's really starting to perform a good foundation with a good backdrop for growth heading into 2021.

So sitting here today, we know and we will -- we need to keep on positioning Titan to navigate through the pandemic and new challenges of today's business climate. Over the past 6 to 7 months, our results have indicated our ability to do just that. Along with managing the operational aspects of fluid, very fluid business environment as being heavily shaped by COVID, we will remain committed to managing our balance sheet to not only get through the crisis but position ourselves for expected future growth.

Looking beyond 2020, we believe that the continuing positive actions here at Titan, our development of new and innovative products, combined with the underlying improvements in market conditions, should drive good financial improvements and put us in a strong position for the refinancing of our 2023 bonds.

I want to close by once again just expressing my appreciation to the One Titan team and our thousands of employees around the world working hard every day to manufacture our products. And so with that, I'd now like to turn the call over to Dave.

**David Martin:** Thanks, Paul, and good morning to everyone participating on the call today. Several things really stand out with respect to what is happening in the business over the course of this pandemic. Economic impacts are abundant across all the markets we serve, but we have managed to push through with great resolve.

As Paul discussed earlier, we're building an improved foundation for a brighter future for Titan as the markets recover. I'll get into some detail regarding this quarter's financial performance in a minute, but I want to review the most important things here at the outset.

First, operating cash flow during the third quarter was stellar at \$42 million, helping us to bring global cash balances to almost \$99 million. Second, with the improvements in cash flow, both from an operating perspective and from the additional sources of noncore asset transactions, we lowered debt levels to the lowest level since mid-2018. And now net debt now stands at \$366 million, an improvement of \$67 million from the end of last year. Third, the gross margin improvements, coupled with operating cost control that we've done, have enabled us to increase our financial performance over the prior year with adjusted EBITDA improving by 68% in the third quarter from last year.

Finally, the slope of the decline in sales that we've seen throughout 2020 has diminished somewhat during the third quarter, with almost half actually coming from currency devaluation. And we're seeing positive trends as we head towards next year.

Now let's review the details of the quarter. Net sales for the third quarter were slightly improved over what we expected at the beginning of the quarter as Q3 normally represents a seasonal low in the business. That was certainly true, but we also saw an uptick in the drop-in orders, which translated to sales improvements toward the end of the quarter.

Net sales declined 12% or \$41 million less than the third quarter last year but were \$19 million improved over the second quarter. We estimate the direct impact of COVID-19 effects on net sales was \$8 million in the third quarter, meaning the impact from plant closures in disruptive markets in Europe and Asia.

On a constant currency basis, revenues would have been down only 6% from the third quarter of 2019 or \$21 million. The negative currency impact was approximately \$20 million or 6% with much of the

impact coming from Latin America and Russia. Again, this quarter, the largest impact on sales was in the Earthmoving/Construction segment where sales declined by \$32 million from last year.

The drivers of the decline in EMC were across the board, with the biggest impact coming from North America and ITM business. The remaining declines were primarily in the U.K. and Australia. Agriculture net sales were down \$3.6 million or 2.3% with \$13 million coming from currency impacts, which again is a testimony to the resiliency of the AG market with an increase in volume during the third quarter.

The consumer segment experienced a decline of \$5 million in the quarter, reflecting primarily U.S. sales and specialty markets where we had deemphasized certain product lines in recent months. The utility truck tire sector in Latin America actually rebounded during the third quarter after several consecutive quarters of decline.

Our North American sales were down relative to last year, while we have generally seen the agriculture sales on par or improved in recent months. The areas of decline has mostly come in the construction and earthmoving markets. Our aftermarket tire sales in North America in Q3 were up relative to the prior year, and year-to-date are very close to the 2019 levels at the same point.

Another major highlight for the quarter relates to our Latin American operations. While reported sales were down 3.6% for the quarter on a constant currency basis, sales would have actually increased by 29%, reflecting a strong rebound in demand, particularly in the AG segment in Brazil. As Paul described earlier, the market is coming back strong after weakness that was brought on rapidly by the pandemic in the first half of the year.

Our Russian sales were down 13% from the prior year, but currency headwinds were the entire story as volume and pricing were slightly favorable compared to the prior year. The overall market conditions haven't changed dramatically with continued depressed economic conditions in the region, but we continue to perform at or better than the market and dealer sentiment is also currently positive.

Our overall sales volume on a consolidated basis was lower by 10% from last year. Price and mix in the third quarter was positive at 3.6% in the quarter. Improvements in gross profit remain one of the key stories for us this quarter. Gross profit for the third quarter was \$31 million versus \$27 million in the third quarter of 2019, representing a 15.6% improvement, despite a decline in sales.

Our gross profit margin for the third quarter was 10.3% versus only 7.8% last year. This performance was also in line with what we experienced in the second quarter this year. Tailwinds on raw materials

remain the primary driving factor in our improvement year-over-year, while we have made nice improvements in reducing our overheads in response to the downturn in sales and ongoing production levels.

It's important to note that while raw materials are a positive factor, our customer pricing also moves in relative tandem, making it very important for us to manage our other cost of production, which we have done this year.

Let's move over to segment performance. The Agricultural segment net sales were only down \$3.6 million or 2% from the third quarter of last year. The reality is we saw organic growth of 6% in the quarter. Currency translation was significant and affected sales by almost 9%, primarily in Latin America and to a lesser extent, Russia.

Volume in this segment was up 2.3%. And while we had also picked up in pricing and mix of 4%, similar to the Q1 and Q2 impacts. Our aftermarket sales have continued to be strong, and there have been positive impacts from selected price increases.

Our AG sales overall in North American tire were up 2.8% for the quarter as aftermarket trends remained strong, partially offset by some OE customers continuing to drive the lower production. Our OE wheel sales in North America were down somewhat in the third quarter as well. Russia's AG sales levels were virtually flat year-over-year, while the European AG sales were up almost 29% to last year.

One of the most significant impacts or highlights for the quarter related to the Latin American AG market, which I alluded to earlier. Reported AG sales for Latin America were virtually flat to last year, but volume was up 23% in the third quarter with lower currency levels, wiping out all those gains.

The market has rebounded significantly in the second half of the year, and the trends are looking strong for the near-term market demand, including the first half of next year. While a smaller component of overall sales performance, Australia also saw nice increases in AG sales in the quarter compared to last year, as market conditions have improved from better weather conditions, as well as, stimulus coming from the government.

The agriculture segment gross profit for the quarter was \$16.2 million, up from \$10 million last year, representing a 55% increase. The gross profit margins in the third quarter were 10.6% for AG, which was an improvement from the margin produced in Q3 of 6.7% and also similar to the reported result in the second quarter.

We discussed this last quarter as well, but we have seen improvements in plant efficiencies from the strong internal actions we've taken, along with lower raw material costs, enabling this improvement. A key component of this improvement came from North American wheel operations, which delivered strong results in the third quarter as we continued to improve the operations after significant headwinds that existed in 2019 surrounding raw material and inventory management.

The turnaround accelerated in the third quarter for this business. That said, each of our geographic businesses experienced expansion in gross profit and margins in the third quarter compared to the prior year.

Our Earthmoving/Construction segment continues to see the most impact from the challenging year that we faced being not hit only from the economics caused by the pandemic, but also the global construction slowdown. Overall, the EMC segment experienced a decline of \$32 million or 21% from the third quarter of last year. On a constant currency basis, net sales would have decreased 19% for the quarter versus last year, which meant that currency was really only a minor impact in the quarter.

Volume was down in the EMC segment by 19.4%, while price and mix were almost negligible at 0.1% favorable impact. North America saw the largest decrease year-over-year with a decline of \$14 million. ITM's undercarriage business continues to be impacted as well in the segment with a decline of \$11 million from last year. As a reminder, this business has significant operations in Europe, and activity in Q3 tends to be lighter due to the holiday and vacation season, which has been more impactful this year due to the extenuating circumstances that we live in.

In the recent months, we've seen improvements in the order book for the ITM business, and indications are favorable for the markets in the upcoming period. Gross profit within the earthmoving and construction segment for the third quarter was \$12.4 million, which represents only a \$526,000 decline from a year ago. The gross profit margin in the EMC segment was 10% versus just over 8% in the prior year.

With lower sales, margins could have been stressed but we expanded margins by controlling our production costs very well. In addition, raw material costs continue to be a tailwind for us relative to the prior year.

The Consumer segment's Q3 net sales were down 15% compared to Q3 last year. The negative impact from currency translation was 12% for the quarter. Volume decreased by 20.8% and pricing mix were



favorable at 17%. The largest negative impact from a volume perspective was in North America as demand dropped significantly due to market economics but also the de-emphasized specialty product lines. Demand in Latin America related to the utility truck segment was improved, but currency devaluation wiped out all these gains in the quarter.

The Consumer segment's gross profit for the third quarter was \$2.7 million, similar to the first and second quarter results but declined \$1 million from a year ago.

Gross margins were 9.5%, which was a decline from 11% last year. Again, this has -- entirely really relates to the mix of products sold.

Let's move over to our SG&A cost. SG&A and R&D expenses for the third quarter were \$35.7 million, but this included \$5 million from the legal accrual for the anticipated litigation segment settlement of the long-standing DICO case, which I will discuss in a few minutes. If you exclude the legal accrual from these costs, we spent \$30.7 million, which was in line with our Q2 spending levels and 12% below the third quarter of 2019 adjusted spending level of \$35 million after you exclude the ITM IPO costs that were expensed last year.

Again, this decline came as a result of concerted efforts across the business to control costs. The largest areas of decline came from lower employee-related expenses, including travel as we continue to contain costs across the organization. Similar to Q2, we also managed our sales and marketing costs and our IT spending and investments that we make.

I expect our SG&A costs to continue to be on a fairly tight band around this level, while Q4 levels may be somewhat higher due to the timing of certain initiatives. If you exclude the \$5 million impact from the legal settlement accrual in the third quarter, we continue to be on pace for full year SG&A and R&D costs around the low end of the previous range I discussed of \$130 million to \$135 million.

Now just a bit more on the \$5 million legal accrual. We move forward to settle the long-standing DICO property litigation with the federal government. This litigation has been outstanding for many, many years. And it is in our best interest to resolve this for Titan and for the city of Des Moines and all parties involved. This matter is more fully described in the 10-Q, but we anticipate final settlement in the near term, which would require a payment of approximately \$11.5 million once the court takes the next step to issue the final order, and then we obtain all the necessary government approvals.

While we continue to have significant impacts from currency fluctuations on our P&L, the currency revaluation impacts on intercompany loans was fairly muted in the quarter. We had a foreign exchange loss in the third quarter of \$1.3 million versus a loss last year of \$2.3 million.

We recorded tax expense of only \$342,000 in the third quarter on a pretax loss of \$13 million. Our expectations for the full year taxable income in non-valuation allowance jurisdictions have been reevaluated this quarter, which resulted in lower taxes recorded in the quarter.

Now let's talk Q3 cash flow. We have made strong strides relative to our balance sheet and the overall liquidity picture in the midst of a challenging year, particularly this quarter. I'll start with the fact that cash ended at \$99 million, up \$18 million from the second quarter and up almost \$32 million from last year-end. Cash levels are at the strongest since mid-2018.

Most importantly, this increase came from strong operating cash flows in the third quarter. We generated approximately \$42 million in operating cash flow in the third quarter, one of the best quarterly performances in many, many years. Year-to-date, we have now generated \$47 million in operating cash flow. Including the impact of the final sale of shares in Wheels, India of \$17 million early in the third quarter, we generated free cash flow in the third quarter of \$54 million.

I continue to have confidence in our ability to generate cash from improvements in working capital for fiscal 2020, excluding the effects of lower sales volume that will come from continued improvements in inventory management across the business. As you see in our cash flow statement for the first 9 months, working capital has been a source of cash flow of approximately \$44 million, which is partially due to lower sales volume, as I mentioned earlier.

Lower inventories have been a \$37 million source of operating cash flow in this time period as well. We had strong focus with our operating teams to manage inventory very closely and collectively know that there's a balance to manage due to the lack of long-term visibility of customer demand, which is very challenging for us, but we are managing through.

We remain focused on having the necessary production levels and inventory in place to meet customer expectations for timely delivery.

Capital expenditures for the first 9 months of 2020 reached \$13.4 million, which reflected continued control of investments in the midst of the pandemic. This compares to \$26 million last year for the first 9 months. We have continued to tightly manage our capital spending programs and to invest where it is

important to manage production, maintenance of our equipment and the safety and welfare of our employees.

Of course, we can't hold these investments back forever but has been prudent to manage cash very carefully during this time. We do anticipate spending to increase next year, but only as we see sustained improvements in our markets and the business. We will continue to bring innovative products to the market to be competitive and maintain our market leadership. I've discussed this many times before.

For this year, we will maintain the expectation of full year capital spending of approximately \$20 million with 1 quarter to go. Our overall debt level decreased by almost \$39 million from the end of June to the end of September. As of September 30, there are no borrowings on the domestic ABL credit line as a result of the strong operating cash flow and the results of the noncore asset sales.

Short-term debt at the end of September was \$32.6 million, which is down by over \$29 million since last year-end and \$8 million from June. This decline is due to the repayments of normal maturities of the loan arrangements in certain of our foreign operations, primarily Russia and Europe. A portion of this plan also related to extending a loan in Latin America 1 year in response to the liquidity initiatives late in March this year.

Our debt levels have not only declined this year, but the complexion of our overall long-term debt has improved as well with measures we took in Europe, Latin America and Russia, with our banking partners to secure facilities that are more flexible and cost-effective for our operations.

Cash flow was strong across all of the international operations in the third quarter, which added to the flexibility for our business to manage for the future, along with the actions we've taken throughout the year. We now have more flexibility to manage our U.S. and corporate operations as well. We freed up the borrowing capacity on the domestic credit facility, and we've been able to maintain our good solid cash flow in North America.

Currently, the borrowing capacity when you take away the letters of credit and adjusting for the borrowing base calculations of AR and inventory, our capacity is at \$61 million at the end of September. We continue to pursue transactions surrounding some discrete noncore assets representing approximately \$16 million to \$20 million in additional cash flow.

We made more progress on these items in the last 30 days, and I anticipate completing these transactions during the fourth quarter, which will further benefit our financial flexibility.

To wrap up, we continue to make nice progress on our path to stability as a company during this last quarter, notwithstanding the turbulent times that we move in. This is paramount for us as we head into what we hope and believe will be a brighter market ahead.

Our financial position is improving. I will restate it again, cash has increased by almost \$40 million since Q1, and our net debt is down by over \$67 million since last December. This is very important as we progress towards 2023 and the maturity of our bonds and the flexibility we need to manage our business and manage the refinancing decisions.

We are taking care of both our liquidity and how we manage our business to see top line and bottom line improvements in the future. As I said continually on these calls, there is much work to be done to position us for the long-term future, but I am pleased with our progress so far. This race doesn't have a finish line, and we are continuing to run hard.

That concludes my remarks. And so I'll turn it back over to the operator for any questions you have.

### **Question-and-Answer Session**

**Operator:** (Operator Instructions) Our first question today comes from Joseph Mondillo with Sidoti & Company. Please go ahead.

**Joseph Mondillo:** Thank you. Good morning, everyone. Just a question on your guidance first. It looks like it implies a tick down from the third quarter in the fourth quarter. Is there anything there beyond the normal seasonality that we usually see in the fourth quarter?

**David Martin:** No, not really, no. We have to be very prudent as to how production levels go in late November and December. And it does play havoc with the scheduling and so forth. So there is traditional seasonality going down in particular, here in the EMC segment. So we were just being very prudent about that guidance in Q4. It's also managing towards the beginning of what will be our busiest quarter in Q1. So we're trying to manage the schedules very tightly right now.

**Joseph Mondillo:** Okay. And I guess the second question would be related to the pandemic. I'm assuming in North America right now, operations are running smoothly, but Europe, we're hearing

about partial sort of lockdowns. What are you seeing, I guess, maybe primarily in your European operations and the overall pandemic? And how that may affect 4Q and maybe potentially 1Q?

**Paul Reitz:** Yes. I mean, it's something we're obviously watching really closely on a daily basis. And as I noted in my comments, I mean there are some concerning trends that can't be overlooked. However, you kind of look back to where we're primarily located in Europe with 4 plants in Italy and Spain and then up there in the U.K. We've been through pretty hard times already, and we've been managing through the heart of the crisis over there since March. We've seen and continue to see good government support even this morning, the U.K. put out some additional announcements on support they're going to put into the marketplace. And so I can't speak on behalf of the government, but I do think you see in Europe a stronger unification within their countries to support the economy. They're able to take quicker actions to do that than what we see here in the U.S. . And so I approached this quarter and then going into next year with a level of concern, but also a stronger sense of optimism that we will find our way through it. There's good demand that's out there, and I think the local government officials and the national government officials realize that they just can't turn the economies off. And so we will operate safely. We will do everything that's required and make sure our employees are safe on a daily basis, and that does require some additional costs, and you do take on some additional inefficiencies. But at this point, I don't think we have anything that would cause us to believe that we can continue to see some good growth going into not just this quarter but into next year.

**Joseph Mondillo:** Okay. And just to clarify, all your operations are sort of fully operating currently?

**Paul Reitz:** That is correct.

**David Martin:** Yes, we're certainly operating under the protocols of the restrictions that are mandated by the local authorities, but we are managing and are open.

**Joseph Mondillo:** Okay. And I just wanted to shift to sort of the overall AG environment or sentiment. You mentioned farming sentiment is up to a 5-year high. I'm just curious on how you measure that. or what metric you're looking at relative to that? And related to that, we've seen corn prices tick up over the last 4 or 5 years, reached the \$4 mark a few times, and then we've seen it sort of come right back down. It sounds like maybe this time around there's invasion that maybe it will be a little stronger than we've seen when corn prices have bounced up to these levels before. Could you just give us maybe some more color on how you're feeling about the overall AG market as we go into '21?

**Paul Reitz:** Yes, absolutely. I mean the [7] levels that we measure are different services we subscribe to along with the national polls that are out there. So we follow closely and always have. We're not doing it just because we're in the middle of a pandemic, what's going on with the dealer sentiment and the farmer sentiment. We're really starting to see the positive nature being expressed within both farmers and dealers. It is coming from the price of commodities. And like you said, corn has hovered up and down around that \$4 mark, so means has done better. But really, what we see is the main driver, Joe, is inventory levels. Across the board, we're seeing inventory levels in AG that are just at extremely low levels. And so it doesn't take much optimism within the space. And I think there's enough optimism that exists when corn is in that \$4 range combined primarily with the low inventory levels that give us the sense of confidence that next year is going to be a year of growth. I mean, the inventory levels with some of our primary customers that we track closely just almost historical levels -- historical low levels, I should say, and just replenishing that will drive some growth. And then you throw in the government incentives on top of it, which I think are consistent. We talk about it on a regular basis. But what government, what economy right now can't support their people through their agriculture economy, and you're seeing it the \$14 billion that's being put into the farmers' pockets just here in North America by the end of the year. And I think that's a consistent trend you may see around the world. In April, David mentioned it and I mentioned it, it's how on top of it Brazil, Brazil is just red hot. It gets kind of muted sometimes by the currency and all the other movements associated with that, that impact the financials. But from a business perspective, demand is strong in Brazil. It's solid in Europe, and I think it's got a strong position to continue to go on an upswing in North America. But to answer your question, though, is the dealer inventory levels are really the -- I think could be one of the primary drivers for next year.

**Joseph Mondillo:** Okay. Great. And then one last question, and I'll hop back in queue. Just related to cash flow. I think, David, you mentioned \$16 million to \$20 million of further noncore asset sales expected to be completed potentially in the fourth quarter. Are there any other sort of noncore assets as we look into '21 that you're looking to sell? And then you've also talked about some underperforming businesses. Could you update us on that? And then just lastly, related to free cash flow. In an upturn environment, how do we think about sort of free cash flow? Because depending on how strong the upturn would be, you probably have to invest in working capital and CapEx has been at low levels. So I'm just curious if you would anticipate operating maybe in the initial upturn on a negative free cash flow basis. Just wondering what your thoughts are on that.

**David Martin:** Yes. Great questions. I'll start with the noncore assets. The \$16 million to \$20 million represents very discrete up transactions that we're working on, the very, very distinct. We continuously are evaluating the assets that we have in place and things like that and some of the noncore operations or assets. And those things will continue. That's a never-ending process for us, but they're not included in the \$16 million to \$20 million, so we will be continuing to look at those things well beyond 2020. Again, I feel very confident on the \$16 million to \$20 million because of the progress that we made on some of these -- some of these transactions. So we'll move on from that. Great question with respect to what we're looking at for next year as recovery happens. Yes, I do expect that there's obviously going to be further investments in working capital, particularly obviously inventory would be a key one as we need to have inventory in place to be able to manage customer expectations and so forth. There will be some investment there. I don't think it's going to be dramatic; one that will create stress for us per se, because I think it will turn on over time. So we're going to manage that very carefully. The same goes with investments in capital expenditures. We will not just turn it off -- turn it on overnight. We'll be managing it prudently so that we can maintain free cash flow that's at least neutral or positive. That's the goal. And so we're going to be really, really focused hard on that and trying to manage that very carefully with our business unit managers.

**Operator:** The next question comes from Komal Patel with Goldman Sachs.

**Komal Patel:** Hi Good morning. Thanks. We hit on a lot of points that I wanted to touch on, but maybe a follow up on the farmer sentiment. I guess just given the political landscape, can you add some color about some of the implications for farmer sentiment or incomes into '21 based on kind of some of the different political outcomes, whether kind of a democrat President mixed legislature. How do you think there could be any influence there into next year?

**Paul Reitz:** Yes. I think from a political standpoint; we are very fortunate to be in the industries we're in now. You talk about the size of the infrastructure builds and different government programs varying by depending on which party's in control. But I think we're very fortunate the industries that are in that governments have to support and whoever is in charge, you can't ignore construction, you can't ignore infrastructure, and you certainly can't ignore agriculture. And so the payments for this year are already locked in. But I don't see a divided house incented and president having an impact on the fact that you guys take care of your people through agriculture. And so I think we almost get to live in a nonpolitical world in the industries that we serve, and we all got to unite together in making sure we take care of these spaces, and I think they will. And I think the pressure -- the European comments that I made, I

think, are important as well to put pressure on North America. So regardless of whatever is going on with our situation, when you have the European governments taking quicker, swifter decisive actions to provide support for AG and infrastructure, it certainly puts the pressure on our politicians to make sure they're doing the right thing for their people as well. So yes, is there a risk? I can't sit here today and tell you there's not, but I think it's a list that's fairly mitigated.

**Komal Patel:** Okay. That's fair. That's really helpful. And then maybe just the second thing. I wanted to check in on minimum cash target and leverage. Given that the business is on better footing now, can you remind us on minimum cash balance? And then how quickly you think you can get to your leverage target of around 4x?

**David Martin:** Great question. We've managed very, very well through the year. Obviously, our cash balances have come up. There's a minimum cash balance of around \$55 million to \$60 million. That's where we were managing obviously last year and early this year. I don't expect that we're going to have to -- either we're going to see negative cash flow to the extent that gets us down in those levels at all. The key thing is that we've taken the steps on the debt levels to manage those very well. The majority of our debt is obviously the bonds. So there's not going to be a lot of movement on the debt side. The truth of the matter is it has to be in earnings. And so we've taken also the necessary steps on earnings as the markets recover, and the margins that we should achieve in the future should get us to those levels sooner than later. As far as a specific time frame for getting to, call it, the 4x is -- it's certainly a target of ours, and it depends on a little bit on when the markets recover as well. But we do have internal actions that are also being taken on these underperforming assets to be able to eliminate the drag that they create. And we're looking to get those -- all the actions we want to take are all now in 2021. So as we get out of 2021, that drag that we see has to be gone. And then it's just a matter of where our markets are in our performance in it.

**Operator:** (Operator Instructions) The next question comes from Kevin O'Brien with Imperial Capital.

**Kirk Ludtke:** This is Kirk Ludtke from Imperial. Can you hear me?

**Paul Reitz:** Yes.

**Kirk Ludtke:** As the outlook improves, can you give us an update on some of those initiatives you've been talking about to boost utilization rates and where those stand? Are they still a priority? What type of gating factors there might be?



**Paul Reitz:** Yes. I mean it's something we definitely still see as a priority. There's changing circumstances with demand. We are constantly, I guess, looking at those is the best way to put it. And as far as decisions being made, we have not reached that point. But there are challenges associated with kind of some of our capacity utilization because each location will make different products. And so you have to look at it from the perspective of either transferring products and/or introducing new products to improve your capacity utilization or ceasing the production of products. And so the long-winded answer is to basically say, yes, it's still a priority. It's something we're continuing to look at. And clearly, as we close out this year and look into next year and we do our 2021 planning, there will be a topic that will be discussed -- is being discussed quite heavily with management already and we discussed with the Board at the end of the year as well.

**Kirk Ludtke:** Okay. Could you give us an update on LSW? And how the take rates might have changed? And when that might really start moving the needle?

**Paul Reitz:** It has moved the needle. LSW is by far the most innovative product that comes into the agricultural industry. I'm going to throw some of my hurdle out there has been really the history of our space. I mean, we completely redefined AG tires and wheels, just like you see in the SUVs on the road today. If we didn't have low sidewall on SUVs, we wouldn't be driving them. They'd be bounce up and down the road. And so we have revolutionized how equipment performs and through the wheels and tires that redesigned with LSW. So yes, it has moved the needle. We have been and we continue to be extremely impressed with the performance of the product, which is most important. You got to drive the value to the end user but also the sales and the margin profile on LSW. And so where we've seen a difference perhaps, where we would be selling LSW is we are selling a lot more directly to our tire dealers and directly into the end-user market versus through the OEMs. And so the only question I think out there for the future is, what else we can continue to get the OEMs to sell. Now clearly, they have a different perspective on LSW, because they also manufacture tracks and the quad-tracks, et cetera. But yes, we were extremely impressed with how LSW continue to perform. So it has moved the needle. But I also want to highlight the fact that it isn't just about LSW. I mean we have a number of new product ranges that have introduced in South America already that are moving the needle. And here in the U.S., we introduced a major new product last year -- or excuse me, this year, that will drive sales into next year. Then as we round out this year, we have another couple of new product lines that are being introduced for next year. So it's a cost evolution has moved way beyond just LSW. But LSW is still the bread and butter of our product -- our new product and development that we put into this space in 5

years. And something that makes equipment perform better is going to continue to sell and our dealers continue to accept it at a very, very high rate.

**Kirk Ludtke:** Great. And then lastly, maybe circling back to the question about how working capital might be a use of cash as volumes increase. Can you talk about the initiative to reduce SKUs and how that has progressed and maybe put some numbers on the progress there?

**Paul Reitz:** Yes. I mean it's a good question. It's been a big priority for us as well. It's not just about throwing new products into the plants. We also got to get rid of some ones that are underperforming, and that's something we've been embarking on for the last couple of years. On the tire side of our business, you look at the amount of inventory we now hold in our A products, it's improved significantly. I don't have the exact number in front of me today. Perhaps David and Todd can get back with you later on that. But we are holding the right inventory. So when you look at a company like us managing working capital, managing cash flow, it's driven significant improvements there. But it's also made our plants more efficient. And so what we're able to also do and kind of going back to that capacity utilization topic, we are able to improve our capacity utilization by redesigning them because of the improvements we've made in our product portfolio. So if you go through our largest tire plant that we have in the U.S., you'll see that it's being completely redesigned and roughly 35% of that plant now is being geared up to simply run our highest running best A product every single day, all day long. And so, those type of changes are coming because we made significant improvements to our product portfolio. And so what it does is it continues to lead to further improvement. So it not like the switch that we can just turn on overnight, but it does give us that foundation that we will continue to get more efficient. And that redesign I mentioned at our largest target plant is Phase 1 of 4. And so we'll continue to do that. But it all started by the fact that we've redesigned our product portfolio. As we speak in this quarter, we've made more progress on our wheel business than we have in any point in history, and we got to do more. So I think the wheel business is where we will pick up the biggest benefits that we haven't really utilized or realized yet in 2020. We'll start to see more of that in 2021. They embrace it, they get it, they want to do it. You got challenges with customers. I mean you can't just go to your customer and say, "Hey, we're just dropping this product tomorrow in every single case." Some cases, yes, other cases to have a longer tail on it. But I've been very impressed with our wheel team. In the last, I would call it, David, let say, last 3 to 4 months, I mean they've really embraced it and they're taking strong actions.

**David Martin:** Yes, those actions will benefit us next year. And so yes, it's very good progress.

**Operator:** Our final questioner is Justine Ho with Mesirow Financial. Please go ahead.

**Justine Ho:** Morning. I wanted to ask about raw materials and the trends you're currently seeing or what you're expecting considering, I guess, this past quarter, there were some tailwinds as it relates to better margins because of the lower raw materials?

**David Martin:** Well, good question. Obviously, throughout this year, raw material costs have been lower, as you might expect. The way raw materials flow through our plants, there's a little bit of a lag, obviously, with respect to that. And then there's also pricing. So it's not necessarily a one-for-one kind of a situation. We have to manage that very carefully with our customers as well as our suppliers. And so as demand continues to -- will continue to uptick over time, there would be an uptick in pricing as well. So we have to manage that very carefully, and we are doing so. I still expect that the raw materials relative to historical pricing will be still somewhat favorable to at least on par with that. So as far as what it means from a margin perspective, it will be similar to what we've seen.

**Operator:** This concludes our question-and-answer session. I would like to turn the conference back over to Mr. Reitz for any closing remarks.

**Paul Reitz:** Well, I appreciate everybody's time and participation this morning. I look forward to talking to you again as we report our next quarter's results. Everybody stay safe and stay healthy. Take care.

**Operator:** Please note that a webcast replay of this presentation will be available soon within the Investor Relations section on our website under News and Events. Thank you for attending today's presentation. The conference has now concluded.