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DXP Enterprises, Inc. (DXPE)

Q2 2019 Earnings Call

CORPORATE PARTICIPANTS

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Joe L. Mondillo
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Blake Hirschman
Analyst, Stephens, Inc.

Ryan Mills
Analyst, KeyBanc Capital Markets, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon. My name is Rishane. I will be your conference operator today. At this time, I would like to welcome everyone to the DXP Enterprises, Inc. 2019 Second Quarter Conference Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions] Thank you.

Mr. Yee, you may begin your conference.

Kent Nee Hung Yee
Chief Financial Officer & Senior Vice President, DXP Enterprises, Inc.

Thank you, Rishane. This is Kent Yee. And welcome to DXP's Q2 2019 conference call to discuss our results for the second quarter ended June 30, 2019. Joining me today is our Chairman and CEO, David Little.

Before we get started, I want to remind you that today's call is being webcast and recorded and includes forward-looking statements. Actual results may differ materially from those contemplated by these forward-looking statements. A detailed discussion of the many factors that we believe may have a material effect on our business on an ongoing basis are contained in our SEC filings. DXP assumes no obligation to update that information as a result of new information or future events.

During this call, we may present both GAAP and non-GAAP financial measures. A reconciliation of GAAP to non-GAAP measures is included in our earnings press release. The press release and an accompanying investor presentation are now available on our website at ir.dxpe.com.

I will now turn the call over to David to provide his thoughts and a summary of our second quarter financial results.

David R. Little

Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.

Thanks, Kent, and thanks to everyone on our 2019 second quarter conference call. Kent will take you through the key financial details after my remarks and after our prepared comments, we will be open for a Q&A session.

It is my privilege to share DXP's second quarter results with you on behalf of over 2,723 DXPeople. Congratulations to all our stakeholders and a special thank you to our DXPeople you can trust. We are pleased to announce strong second quarter results with sales, operating income and earnings per share all up over the prior year. This was a great way to follow up our strong first quarter as we move into the second quarter of fiscal 2019.

Like many companies, we are dealing with the challenges of facing uncertain trade policies and other macro factors. However, through our strong customer focused orientation with our businesses, we provide products and services that help them save money, consolidate their MRO spend, manage their inventories, provide solutions to improve their processes and we help keep their operations running and people safe. We are investing in DXPeople and for sales growth to gain market share regardless of the point of the economic cycle.

So far this year, we have delivered strong operating results in the first half of 2019. Year-to-date through June 30, total sales were up 7.9%, operating income is up 20.7%. Total sales for the second quarter grew 7.1% to $333.3 million and we were able to deliver 16% diluted earnings per share growth over the prior year quarter. Each of our three business segments improved sales sequentially with segments' operating income margins in line with our expectations.

While some of our key indicators show deceleration, we were able to take market share, maintain operating efficiencies and deliver on our goals and expectations. Sales growth year-to-date have been driven by Supply Chain Services up 15.9% compared to the same six month period in 2018. We continue to roll out new sites and add end-market diversification to DXP. Innovative Pumping Solutions continues to perform and it is up 8.9% versus the same period in 2018. This is considerable growth, given the strong sales performance across IPS last year. Projects that we are benefiting from include pipeline, natural gas and onshore loading stations.

Moving to our second quarter results, total DXP revenue of $333.3 million for the second quarter of 2019 was a 7.1% increase year-over-year. In terms of sales increase by business segment, I was pleased with the contribution of all three segments, with the greatest increase year-over-year coming from Supply Chain Services, which grew 20.6% to $52.3 million. Innovative Pumping Solutions sales increased 9.1% year-over-year to $81 million, while Service Centers sales increased 3.3% year-over-year to $200 million. Overall, our continued growth is great to see.

Supply Chain's growth reflects the additions of new customer sites. They have implemented 12 new sites since Q3 of last year, and including customers in the medical device, aerospace, and food and beverage markets. Innovative Pumping Solutions sales increase continue to be driven by modular packaged equipment for onshore markets and products sold into the midstream markets. In terms of the strength in the IPS backlog, we are up 6% on a quarterly average backlog versus this time last year, and up 16.9% compared six months average backlog. The Service Centers year-over-year sales growth was primarily driven by increases in our rotating equipment and our metal working product divisions. Within Service Centers, we saw particular year-over-year sales strength in the West, Texas Gulf Coast and Ohio River Valley regions.

DXP's overall gross profit margins for the second quarter were 27.6%, a 25 basis point improvement over 2018 and sequentially, an increase of 55 basis points. Specifically, IPS experienced a 519 basis point improvement sequentially. As we discussed in Q1, we expected to see improvement in Q2.

SG&A for the second quarter increased $4.1 million versus Q2 of 2018. SG&A as a percent of sales declined 16 basis points going from 20.9% in Q2 of 2018 to 20.74% in Q2 of 2019. SG&A continues to reflect our investment in our people and organization. As always, it is my privilege to share DXP's financial results on behalf of these DXPeople.

DXP's overall operating income margin was 6.9% or $22.8 million, which includes corporate expense and amortization. This reflects a 40 basis point improvement in margins over 2018. That being said, we still feel that there is opportunity in our operations to be more efficient. IPS' operating income margins were 14.8%, Service Centers operating income margins were 11.6%, and Supply Chain Services operating income margins was 7.2%.

Overall, DXP produced EBITDA of $29.7 million versus $26.6 million in 2018 adjusting for a one-time associated sale of our corporate facility. This turned into a year-over-year increase of $2.1 million or 7.8%. EBITDA as a percent of sales was 8.6% of sales, essentially flat to Q2 2018.

While we are encouraged by our performance in the second quarter, we are continuing to plan thoughtfully for the second half of the year given the uncertain macro environment in which we are operating. We have seen slowing in some of our key indicators that has been overcome by our growth strategies designed to take market share. I am very pleased by our performance in the first half. We still have substantial work to do to achieve our goals and I am confident that the team will continue to execute.

We feel that the economy is still growing and that our goal is to execute on our growth strategies to exceed market performance. We also expect to drive strong SG&A leverage, manage working capital and create free cash flow.

With that, I will now turn it back over to Kent to review the financials in more detail.

Kent Nee Hung Yee

Chief Financial Officer & Senior Vice President, DXP Enterprises, Inc.

Thank you, David, and thank you to everyone for joining us for our review of our second quarter financial results. Q2 shows that we carried our momentum from the first quarter through the entire first half of 2019. We are growing sales and improving gross margins and our balance sheet continues to be poised for us to be acquisitive.

Strong sales growth within Supply Chain Services, gross margin expansion and improvement within IPS along with strategic investments have been key themes during the first half of 2019 for DXP.

For the six month period ending June 30, 2019, total sales grew 7.9% to $644.5 million and operating income is up 20.7% to $37.7 million. Diluted earnings per share is up 29.3% to $1.13 per share.

Total sales for the second quarter increased 7.1% year-over-year to $333.3 million. Second quarter sales growth was supported by all three business segments. Second quarter sales growth was led by Supply Chain Services, growing 20.6% year-over-year to $52.3 million followed by Innovative Pumping Solutions growing 9.1% year-over-year to $81 million and Service Centers growing 3.3% to $200 million.

Average daily sales for the second quarter were $5.3 million per day versus $4.9 million per day in Q2 2018. The ISM PMI manufacturing index averaged 52.2% for the second quarter compared to 58.7% in 2018. Additionally, the metal working business indexed averaged a reading of 51.5% in the second quarter of 2019 versus 58.2% in Q2 2018.

In terms of oil and gas, the average U.S. rig count for Q2 was down 50 rigs versus Q2 2018. Canada's rig count is down 26 rigs versus Q2 2018. That said, WTI averaged $60 per barrel for the second quarter versus $55 per barrel in Q1. In today's environment, we believe our oil and gas customers are focused on disciplined capital allocation and free cash flow. While this clearly indicates that some of our key indicators are showing a decelerating growth environment, we have strategies designed to take market share and we are executing and winning with these strategies.

Supply Chain Services is leading our sales growth this year accompanied by another strong year from Innovative Pumping Solutions. The sales growth in Supply Chain Services is the result of adding new customer sites within the food and beverage, aerospace, medical device, and oil and gas industries which has been occurring since Q3 of 2018. The roll out of new sites does impact operating income margins over the short-term due to implementation costs, including inventory burn off and the initial hiring of onsite personnel without the corresponding revenue fully ramping up.

Projects within our IPS segment which experienced year-over-year sales growth continue to include pipeline, natural gas, and onshore loading stations, as David mentioned. Regions within our Service Centers segment which experienced meaningful sales growth in the second quarter include the West, Ohio River Valley and Texas Gulf Coast.

Turning to our gross margins, DXP's total gross margins were 27.6%, a 25 basis point improvement over Q2 2018. DXP's total gross margins for the second quarter primarily reflects improvement within our IPS business segment. IPS gross margins improved 419 basis points sequentially and we are seeing an overall improvement in the gross margins on the jobs we have in the backlog.

In terms of operating income, combined, all three business segments improved 42 basis points in year-over-year business segment operating income margins versus Q2 2018. Total DXP operating income increased 40 basis points versus Q2 2018 to $22.8 million. Innovative Pumping Solutions improved operating income margins 278 basis points to $12 million, while Service Centers improved operating income margins 29 basis points to $23.2 million. Supply Chain Services decreased 278 basis points year-over-year, and as we discussed, it was primarily driven by the implementation of new SCS sites as we mentioned during our Q1 conference call.

Turning to EBITDA, EBITDA was $28.7 million in Q2, up 2.7% from 2018. However, during 2018, there was a one-time gain associated with the sale of a corporate facility. Adjusting for this gain, EBITDA grew 7.7%. Year-over-year, EBITDA margins were essentially flat or increased 6 basis points after adjusting for the one-time gain. For the six months, this translated into 1.5 times operating leverage and for the quarter, 1.1 times operating leverage after adjusting for the one-time gain.

In terms of EPS, our net income for Q2 2019 was $13.5 million. This is up $1.9 million or 16.4% versus Q2 2018. Our earnings per diluted share for Q2 2019 was $0.73 versus $0.63 in Q2 2018.

Turning to the balance sheet. In terms of working capital, our working capital was $241.5 million at the end of the quarter. This amounted to 19.1% of last 12 months sales. This is above our historical average, but reflects the seasonal nature of working on projects and investing in the associated working capital on project-related jobs within IPS. We expect this to start trending downwards as we move into Q3 and Q4.

Accounts receivable were at $210.3 million at the end of the second quarter, up $13 million sequentially. Inventory is up $13.1 million from Q4. This reflects DXP carrying high levels to support our revenue growth and investment we expect within IPS and the Service Centers. We achieved inventory turns of 7.1 times.

In terms of cash, we had $25.5 million in cash on the balance sheet at June 30. In terms of CapEx, CapEx in the second quarter was $6.3 million or 1.9% of second quarter sales. Compared to the second quarter of 2018, CapEx dollars are up $1.5 million. CapEx during the quarter reflects investments made within our facilities including our corporate office, fabrication facilities in Houston, and other Service Centers locations. We also are continuing to make investments in software to enhance our corporate support operations.

Return on invested capital or ROIC at the end of the second quarter was 25%. During Q2, ROIC was impacted by the $16.2 million increase of working capital from Q1 to Q2. In terms of our capital structure at June 30, our fixed charge coverage ratio and secured leverage ratio remained at 3.7 and 2.2 to 1, respectively. Total debt outstanding at June 30 was $247 million.

In conclusion, we are pleased with the first half of 2019. We look forward to finishing the year strong, executing on our strategy, growing sales both organically and through acquisitions and driving both gross and EBITDA margins. Momentum has been good and we look forward to pushing this through the entirety of 2019.

We will now turn the call over for your questions.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question from the line of Joe Mondillo with [ph] Sidoti & Company (00:17:44).

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Hi guys. Good afternoon.

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.

A

Hey, Joe. How are you?

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Good. So I wanted to first start off with IPS. The margin best that you've seen in a couple of years. Just curious how you think about that margin going forward on a run rate basis. And then also in terms of sort of your order trends, you mentioned Kent that you're – I guess the margin and the backlog I guess was good, but how about your order trends over the last several months and how does that backlog look today as we head into August and beyond?

Kent Nee Hung Yee
Chief Financial Officer & Senior Vice President, DXP Enterprises, Inc.

A

Yeah. And I'm sure David will have some comments here, but just in terms of the order trends, in terms of the backlog, David mentioned in his comments, but the backlog is still up on a quarter-over-quarter basis and comparing the six month average basis. So, from that perspective, we feel good. Is the backlog growing at the same pace as we were at this time last year, no. A majority of our growth in terms of the total business obviously came from Supply Chain, but we still feel good with what we see in our backlog in Innovative Pumping Solutions, and you picked up on my comment, which is when we do our quarterly review of the jobs and kind of where we're at, the average gross margin is improving and was improving in Q2 and so that also gives us comfortability kind of as we go into the second half of the year.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Okay. So looking at that sort of 15% or so operating margin at the segment, when you look at max volume and then knowing what you have in the backlog, is that a sustainable run rate for the back half of the year you think?

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.

A

Yeah. This is David. Sure, I think that we had some jobs in the first quarter that we're not quite as profitable as we would like and so I think those issues are behind us. I think our second quarter, we may have picked up a little bit. So maybe there is a percent or something there that's maybe not as doable, but I think that 14%, 15% number is the area where we should be at.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

All right. And then at Supply Chain Services, a couple of things that I would wanted to ask you about. First off, some of your peers have been talking about sort of price realization and just given I guess inflation on related to tariffs and then just given the fact that growth in demand is sort of slowing, not being able to push though fully though the inflated prices that you're getting from your suppliers, are you seeing any issues with that at all?

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.

A

Oh, sure. That's a constant battle with business that's under our contract with cost savings, promises and et cetera. And so you have to work that. The customer doesn't want to give you a price increase. You have proof that your cost of goods sold have gone up. And so you're trying to push that through and that's a battle.

Now, don't mean it can't get done. Does it get done automatically? No. It's negotiations with the customer and that's just part of the business and things we deal with. But, we don't think of anything if that is being really unusual, we don't think of like the customer goes. Well, I don't believe there are tariffs, because there are. So, I think, as long as you have the proof and then you can get them done, but they take a little while.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

And any thoughts yet regarding the new tariffs that are supposed to go in place in September 1? Do you anticipate further challenges related to those?

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.

A

To the best of my knowledge, we don't pay any tariffs. We haven't paid any tariffs. So think about our manufacturing that we represent. They pay tariffs and they had price increases and they passed that on to us and they passed that on to everybody. So everybody's sort of in the same boat.

As it relates to us buying things from China in any real big significant way, we don't do that. And so we do have one pump HP-Plus. We bought some stuff from China, but it's been classified as a non-tariff item. But even if tariffs do come and I assume they will on this last deal that they're going to have tariffs on everything that is bought from China, then all our competition buys from China too. We all buy from the same spot.

So, again, I don't see anything besides the fact that we're going to have our raise our prices, but so will all our competition, and again that's not a big number. It's a pretty small number. So tariffs really aren't affecting us. As it relates to our customers, that's a little different story. We have customers that export a lot of their materials and stop and sell. China is saying we're not going to buy from you, and so they have a demand problem, and so they're not doing as well. And again that's only a handful of customers I can think of, so it's not a real big threat. So I think we're pretty fortunate, we're domestic, we represent the Made in America and so I think we're just real fortunate as a company that none of this is bothering us too much.

Kent Nee Hung Yee
Chief Financial Officer & Senior Vice President, DXP Enterprises, Inc.

A

Yeah, Joe, the only thing I'd underscore there as David said it, but on our rotating equipment side which is our large product division, where we make the branded private label pumps, those are made in America. So if DXP was going to be susceptible, would be kind of obvious in our largest product category, we're just not. We pay attention, we're queued in like everyone else, but I'm not sure right now we have a lot of concerns, obviously it's real time, so everybody is watching, so.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

All right. Great. And then, just last question for me. Curious what you're seeing, so you did – I believe it was 3% revenue growth? Yeah, 3.3% revenue growth at the Service Centers segment. I'm wondering what your same-store growth was. How many sites including the 12 since the third quarter, what number is that at now? Is there any plans to add additional sites in the back half of the year?

Kent Nee Hung Yee
Chief Financial Officer & Senior Vice President, DXP Enterprises, Inc.

A

Yeah. So I think you mixed two things there, Service Centers and Supply Chain Services. But you're right, Service Centers grew 3.3% in the quarter, Supply Chain grew 20.6%. Supply Chain Services since Q3 of 2018, they've implemented 19 sites total. 13 of those sites have come in this year 2019. And we do have some more in the pipeline for Q3. So we expect the growth trend in IPS to continue, but also the counterbalance there is still – there will still be a little bit of pressure on the operating income margins until we finish those implementations or we get more. There's always more in the funnel.

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.

A

So Joe, on...

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Okay.

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.

A

...on Service Centers, those were all same-store sales. That's...

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Okay.

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.

A

There isn't any...

Kent Nee Hung Yee
Chief Financial Officer & Senior Vice President, DXP Enterprises, Inc.

A

There isn't any...

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.

A

Yeah. There is nothing new.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Yeah. I definitely confused that data point. Okay. Lastly, could you just mention sort of the daily sales at Service Centers through July, if you have those?

Kent Nee Hung Yee
Chief Financial Officer & Senior Vice President, DXP Enterprises, Inc.

A

Yeah. What we do is we typically give you the daily sales for the total business for DXP, the average daily sales.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Yeah.

Kent Nee Hung Yee
Chief Financial Officer & Senior Vice President, DXP Enterprises, Inc.

A

So I can give you that trend through Q2, and then we have a preliminary look at July, but given kind of where our earnings call fell this year, I'll call it preliminary, but April we are $5.3 million per day, May $5.3 million, June $5.3 million, and then kind of July preliminarily we're looking around $4.9 million to $5 million, so.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC
Q

Okay. Great. All right. Thanks a lot. I appreciate that. I'll hop back in queue. Thanks a lot.

Operator: Your next question from the line of Blake Hirschman with Stephens, Inc.

Blake Hirschman
Analyst, Stephens, Inc.
Q

Yeah. Good afternoon, guys. First question for me on the IPS segment, certainly it doesn't seem like there was any headwinds on the margins in the quarter, but I know there was kind of a double rent expense dynamic you guys were facing that weighed on the margins at least last quarter due to opening up the new facility. I was curious if that was a drag in on the quarter if that's kind of flushed its way through?

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.
A

That's there, Blake, and then I think we're out of the other building, I want to say at the end of October.

Blake Hirschman
Analyst, Stephens, Inc.
Q

Got it. And then on the gross margins, was there any mix, price/cost, good or bad guys to call out outside of just the IPS gross margins being real strong?

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.
A

No. They were -

Kent Nee Hung Yee
Chief Financial Officer & Senior Vice President, DXP Enterprises, Inc.
A

It was – it was -

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.
A

...Supply Chain's margins have been – the net margins have been going down because their gross margins we had this lecture about passing on the price increases and et cetera, how that's hard to do and our competition obviously finds it hard to do too, but it does get done, it's just not very timely. So I think there's some pressure there. And then on the Service Centers side, I think they've raised margins. So they've consistently – we've kind of been under a program to raise our gross margins in that particular area and so I think they have successfully done that. Small increments, but they've done that.

Blake Hirschman
Analyst, Stephens, Inc.
Q

Got it. Let's see on Canada, I know you've talked about it being kind of tough in the past as far as the market and environment. You guys have been taking some share to offset that. But I didn't really hear much about it in the opening comments. Just kind of curious to get an update if you've seen things ease or get any worse since last quarter and kind of an update on what all you're doing to drive share gains up there.

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.
A

Yeah. So Canada is our – there's two pieces of Canada. There's the rotating equipment and our safety services business and the safety services side is struggled and it's making progress where struggled is that our employees still want to make a lot of money. I don't blame them, but our customers don't want to pay for their services. So that's been kind of a push-pull deal, but we're finally getting where we would like. We're making progress there. And so I think that's a plus. Our pump side is been doing well. They have some markets that are doing good for them, realized too that we're also on the East Coast. So all that's not oil and gas, that's industrial, municipal, Montreal, Toronto, those are lot of water around there and et cetera. So they've done fine. And so really our rotating equipment side has really done a nice job and so it was just a matter of getting the safety service piece worked out. And we feel good about the direction it's headed.

Blake Hirschman
Analyst, Stephens, Inc.
Q

Got it. And then just lastly, any updates on how you think about M&A or how we should think about free cash flow generation for the year just kind of over the next few? Thanks a lot.

Kent Nee Hung Yee
Chief Financial Officer & Senior Vice President, DXP Enterprises, Inc.
A

Yeah, Blake, just in terms of M&A, we're always looking at opportunities in that, that is the case. I'll make a macro comment. I think from an industry perspective, there's been a lot of activity and I anticipate they'll continue to be in the second half of the year and hopefully, we'll participate in some of that.

In terms of free cash flow, the second half of the year is always the better part for us. That wasn't the case last year and that's the case trending for this year. We had cash flow from operations. We are positive in Q2. So, we're actually ahead of where we were last year and so really kind of what caused our free cash flow to go negative was really just our CapEx and that's investment, strategic investment, so we control that. But during the second half of the year, we look to produce kind of that strong free cash flow, so.

Blake Hirschman
Analyst, Stephens, Inc.
Q

Got it. Very helpful. Thank you.

Operator: Your next question from the line of Steve Barger with KeyBanc Capital Markets.

Ryan Mills
Analyst, KeyBanc Capital Markets, Inc.
Q

Good afternoon, guys. This is Ryan Mills on for Steve.

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.
A

Hey, Ryan, how are you?

Ryan Mills
Analyst, KeyBanc Capital Markets, Inc.
Q

Doing good, doing good. Yeah, just I was wondering if you could provide some color on what you are hearing from your oil and gas customers around back half activity levels. Given the color from PBF distributors who reported last week, it sounds like there's a lot of uncertainty out there in regards to the back half.

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.

A

Yeah, we don't play like DNOW and MRC or they are in the pipe, valve and fittings and stuff like that business. And so they're not building as many gathering systems and they're not doing some things that have to do with infrastructure. They'd rather drill a well and [indiscernible] (00:34:12) an existing structure instead of creating a whole another gathering system. So we don't play in that arena. So they're really not a great match in terms of looking at them versus us as a peer group, and so I don't think we should look at it that way.

We're selling pumps that are dealing with the amount of water that those oilfields are producing and they're producing a lot of oil and they're producing a lot of water and they've got to do something with the water and so, we sell the pumps that go to that. So we do a lot of pumps in the midstream market, pipeline type pumps. And so again, we're not dealing with the pipe, that's just steel that's put together in a pipe form and it's more of a commodity, we're actually selling the brains of the operation and things that move the fluid down the pipeline, whether it's oil or gas both, both are good markets for us.

And so, our piece of the oilfield is doing fine. I don't think it's booming. We're not going from 5 million barrels a day to 12 million barrels a day again anytime real soon, I don't think or from 12 million barrels per day to 24 million barrels per day, but the business is good for us in terms of the areas that we play and then we just don't play in the commodity side.

Ryan Mills
Analyst, KeyBanc Capital Markets, Inc.

Q

Okay. And then going back to M&A, have you seen multiples come down given that what appears to be a decelerating growth environment and based off the monthly numbers you gave for your average daily sales that we're seeing deceleration year-over-year in your average daily sales as well, do you feel comfortable pursuing M&A in this type of environment along with where your balance sheet is at now? Or could we maybe see deleveraging becoming more of a focus in the short-term?

Kent Nee Hung Yee
Chief Financial Officer & Senior Vice President, DXP Enterprises, Inc.

A

So the first part of that question was just around multiples. I would say the multiples are just maintained consistent meaning, hey, for the larger transactions, you start to get closely, if not into those double digits. We probably all saw [indiscernible] (00:36:54) for north of little bit of 10 times, 11 times, if you will. And so I think that's consistent with where the market's been.

In terms of how do we spend our capital in the second half of the year in a decelerating growth environment, I think from a DXP perspective, we have over $20-plus million worth of cash on the balance sheet. We tend to produce free cash flow in the second half of the year. Last year, cash flow from operations during the second half of the year was over $43 million. And so I think for our average acquisition size, we have more than enough capacity to do those tuck-in type acquisitions. And so obviously, it's business-specific and we want to see performance and we want it to be a good business, but as long as our general filters are met, I think financial criteria are met, we can easily stomach those onesies and twosies, so.

Ryan Mills
Analyst, KeyBanc Capital Markets, Inc.

Q

Okay. And then last one for me. I just want to dig a little deeper in the EBIT margins for your Supply Chain Services. It sounds like price/cost has been a big driver of the year-over-year decline in the EBIT margins. Is there anything else that we should be thinking about in regards to the performance in the first half from a margin perspective for that segment? And do you expect margins to improve in the back half?

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.

A

So, first of all, I don't think price – well, I'm not sure you said that right. I'm going to say it like this. We've had 19 – I guess I'm corrected, we've had 19 sites that we're expanding into. When we go into those sites, the first thing we do is we spend a lot of money organizing their warehouses, barcoding their warehouses, getting our system hooked up to their SAP system, et cetera, we burnt off a lot of their inventory, et cetera. So we have a lot of upfront costs and very little revenues to show for it for a period of three to six months.

So, we've had an unusual amount of revenue growth, which is nice, but we've also had a lot of additional revenue that's coming that hadn't shown up yet, that's been – existing revenue has been eaten away by higher expenses. So, that's really the big effect, that's driving down their operating income. If they're not doing anything, then they get to maybe 9%, but if they have some growth and they're always adding stores and they have new deals if they're getting awarded, et cetera, then it's not unusual for them to be down in the 8%, but they've kind of had an unusual amount of growth that's driven them down to 7%. So, it's not a big swing but it's more expense than it is that we haven't been able to pass along the price increases. I mean, the price increases haven't held, but it's more than...

[indiscernible] (00:40:26)

Ryan Mills
Analyst, KeyBanc Capital Markets, Inc.

Q

Yep. Thanks for taking my questions.

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.

A

You bet.

Operator: Your next question from the line of Joe Mondillo with Sidoti & Company.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Hi, guys. Just a couple of follow-up questions. First off, at IPS. I'm just wondering what the costs related to the other building, what costs are you still carrying and I guess you said through October?

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.

A

Yeah. It's rent plus utility plus a lot of stuff. I mean it's probably – I'm paying $100,000 a month. That's a guess, it might be $150,000 and probably lower than the $100,000.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Okay. All right. That's good enough. And then, the second half of last year at the Service Centers segment, you saw some pretty good margins. I'm just wondering, is that a tough comp or is that sort of very doable to match or surpass?

Kent Nee Hung Yee
Chief Financial Officer & Senior Vice President, DXP Enterprises, Inc.

A

Yeah, Joe, this is Kent. I think if I remember last year, part of that was a little bit of some benefit from some mix in the second half of last year. And so, I think the answer is, I don't know where mix will necessarily fall out, but their operating incomes were 11.6%. We're at 11.6%. I think with the mix we have today, we ought to be able to – that's usually always our goal is around that 12% range for the Service Centers. So we don't see anything today that wouldn't say that wouldn't continue.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Okay. And then last one, the corporate expense grew quite a bit, a little bit about $1 million or so. Actually, that's sequentially but on a year-over-year perspective, it was up quite a bit. Just wondering what exactly drove that and how to look at that sort of – is that a run rate going forward or usually in the back half of last year, you saw a ramp up actually from even the second quarter, is that seasonally [indiscernible] (00:42:56), is that normal? Just wondering how to look at that $13.4 million or $12.4 million, sorry?

Kent Nee Hung Yee
Chief Financial Officer & Senior Vice President, DXP Enterprises, Inc.

A

Yes, no, there's definitely increase in our corporate SG&A, Joe, so you're correct. Part of that was a revenue increase associated with an expanded corporate facility. Also part of that was some one-time expenses on professional fees that are just categorized as partially on transaction related, partially just kind of some one-time things associated with accounting, and so kind of as we move forward, some of that will remain, but not all of it. So roughly, call it around $300,000 to $500,000 of that is kind of a one-time.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Okay. And is there a seasonal jump in the back half of the year at that corporate expense?

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.

A

Yeah. Well, it goes down.

[indiscernible] (00:43:57)

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.

A

It's starts up. The first quarter is always high. And then it transmit.

Kent Nee Hung Yee
Chief Financial Officer & Senior Vice President, DXP Enterprises, Inc.

A

Yeah. It tends to trend down.

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.

A

And unless if we're growing 20%, and then we have commissions...

Kent Nee Hung Yee
Chief Financial Officer & Senior Vice President, DXP Enterprises, Inc.

A

Commissions and bonuses and all...

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.

A

...but if the business is flat, the expenses would trend down.

Joe L. Mondillo
Analyst, Sidoti & Co. LLC

Q

Okay. Okay. All right. Thanks a lot.

Operator: This concludes today's conference call. You may now disconnect.

David R. Little
Chairman, President & Chief Executive Officer, DXP Enterprises, Inc.

Thank you.