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WDFC - Q2 2014 WD-40 Company Earnings Conference Call

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PRESENTATION

Operator

Good day, and welcome to this WD-40 Company second-quarter 2014 earnings release conference call. Today's call is being recorded. At this time, I would like to turn the call over to the President and Chief Executive Officer, Mr. Garry Ridge. You may begin, sir.

Garry Ridge - *WD-40 Company - President and CEO*

Good day. Before we start, let me remind you that except for historical information, this conference call may contain forward-looking statements concerning WD-40's outlook for sales, earnings, dividends, and other financial results. These statements are based on an assessment of a variety of factors, contingencies and uncertainties, considered relevant by WD-40 Company.

Forward-looking statements involve risks and uncertainties, which may cause actual results to differ materially from the forward-looking statements, including the impact of commodity prices, the introduction of new product lines, and the fluctuating global conditions, including currency exchange rates, both in the United States and internationally. The Company's expectations, beliefs and projections are expressed in good faith, and are believed by the Company to have a reasonable basis, but there can be no assurance that the Company's expectations, beliefs or projections will be achieved or accomplished.

The risks and uncertainties are detailed from time to time in reports filed by the WD-40 Company with the SEC, including Forms 8-K, 10-Q and 10-K, and you are urged to carefully review these and other documents, and to look for updated Company information on our Investor Relations website at www.WD-40Company.com. A reminder that our Q3 earnings conference call will be on July 9.

Thanks for joining us for the call today. Today we reported net sales of \$94.2 million for the second quarter of fiscal year 2014, an increase of 9% over Q2 last year. Year-to-date, net sales were \$189.7 million, an increase of 4% over the prior-year period.

Net income for the second quarter was \$10.3 million, compared to \$10.5 million in Q2 last fiscal year. Diluted earnings per share for the second quarter was \$0.67, compared to \$0.66 for the same period last fiscal year.

Year-to-date net income was \$21.8 million, an increase of 2% over the prior-year period. Year-to-date diluted earnings per share were \$1.41, up 4% from \$1.35 in the prior fiscal year.

Before we focus on the sales results, let's review the progress we've made towards our strategic initiatives. Strategic initiative number one is to grow WD-40 Multi-Use product. Sales of WD-40 Multi-Use product increased by 10% in the second quarter, compared to Q2 last fiscal year.



We grew Multi-Use product sales 16% in the Americas, and 18% in our EMEA segment. Multi-Use product sales decreased 25% in Asia-Pacific, primarily due to China and Asia distributors.

China was lower due to a general slowdown in economic growth, as well as a decrease in our sales, associated with promotional programs. Sales in Asia were impacted by a backlog of orders that we were unable to ship in Q2 of this fiscal year, as we had planned.

We expect to ship these orders in Q3 of this fiscal year. Sales also continued to be impacted by the transition of our marketing distributor in Indonesia, which is one of the larger markets in our Asia-Pacific distributor region.

Our strategic driver number two is to grow the WD-40 Specialist product line. The WD-40 Specialist product line continued to support the brand, with sales doubling over the prior-year second quarter. We experienced strong growth across all three segments, compared to both Q1 last fiscal year, as well as Q1 of this fiscal year.

We released new product offerings in certain markets throughout the second quarter, while expanding distribution of existing products into new territories. We continue to develop new formulations and delivery systems for the future WD-40 Specialist products.

Our strategic initiative three is to broaden our product and revenue base. Our goal under this initiative is to leverage the strengths within our Company, to derive revenue from new sources outside our flagship WD-40 Multi-Use product, and the WD-40 Specialist product line. We launched five new SKUs under our 3-IN-ONE brand at the end of the second quarter in certain markets, and also expanded distribution of WD-40 Bike products in test markets in Australia, earlier in the fiscal year.

Strategic initiative number four is to attract, develop and retain outstanding tribe members. We welcomed eight new tribe members during the second quarter, and have welcomed 22 new members year-to-date. Developing our tribe members is of utmost importance to us.

We commenced our third year of the leadership lab in January to help the next generation develop talents and skills for both their professional growth, and the Company's performance. We also continued with the Tribology University, a program of technical product knowledge that enables our tribe to better converse about the attributes and features of our products. Both development programs are now offered globally, allowing all our tribe members from sales to accounting, from Shanghai to San Diego, to better position themselves for greater opportunity with our customers and within the Company.

Strategic driver, or initiative, number five is operational excellence. This includes the continuous improvement by optimizing resources, systems and processes. Operational excellence is also a key to meeting our ever-increasing customer and regulatory requirements, as well as helping to offset rising costs that help us protect our gross margin.

During the second quarter, we continued to benefit from our aerosol can sourcing project in China and Europe, which both greatly contributed to our gross margin improvement. We also managed a smooth transition to a lower VOC formula in California, to meet the new regulatory requirements.

We also continued our investment and testing of new systems to improve our back office operations, most particularly a major upgrade of our ERP system in EMEA, and a new global human resource information system. Both systems are on track to go live at the end of the fiscal year. Last but not least, we began to implement a new project management system that will help improve visibility, resource management, and tracking of our innovation and renovation projects.

That completes an update of our strategic initiatives, so let's move on to the details of the second quarter and year-to-date results, starting with sales. Sales in multipurpose maintenance products category accounted for 89% of the global sales in the second quarter, with category sales up 11% in Q2, and up 7% year-to-date, compared to the prior fiscal year periods. Products under this category include the WD-40 and 3-IN-ONE brands, as well as some immaterial sales of the WD-40 Bike product line.



By trading bloc, sales of multipurpose maintenance products in Q2 were up 18% in the Americas, up 17% in EMEA, and down 23% in Asia-Pacific, compared to the prior-year period. Year-to-date sales of multipurpose maintenance products were up 9% in the Americas, up 10% in EMEA, and down 8% in Asia-Pacific, compared to the prior fiscal year period.

Homecare and cleaning products category accounted for 11% of global net sales in Q2, with the category down 8% in Q2, and down 11% year-to-date. Brands under this category include Spot Shot, 2000 Flushes, Carpet Fresh, No Vac, 1001, X-14, and the Lava and Solvol brands.

By trading bloc, sales of our homecare and cleaning products in the second quarter were down 12% in the Americas, up 8% in EMEA, and down 7% in Asia-Pacific. Year-to-date sales of homecare and cleaning products were down [40%] in the Americas, down 4% in EMEA, and down 7% in Asia-Pacific, compared to prior-year fiscal periods.

Now let's take a look at the results by segment, starting with the Americas. Sales in the Americas segment increased 12% in the second quarter, and were up 4% year-to-date versus the prior-year period. This segment accounted for 48% of our global sales in Q2, as compared to 46% in the prior-year period.

Total US sales were up 16% in Q2, and up 6% year-to-date. Multipurpose maintenance products sales increased 23% in the second quarter, primarily due to higher promotional activity, and new distribution of the WD-40 Specialist product line, compared to the prior-year period. Homecare and cleaning product sales decreased 10% in the second quarter, driven by Carpet Fresh and Spot Shot, which declined 33% and 21% respectively.

Homecare and cleaning products continue to generate positive cash flow despite the sales decline, with a portion of the decline stemming from our decision to reduce sales of low-margin products and programs which require significant trade discounts. Sales in this category also declined due to decreased promotional programs, competitor and category declines, as well as volatility of orders within the warehouse clubs and mass retail channels.

Sales in Latin America were up 20% in Q2, and are up 9% year-to-date, driven by higher WD-40 sales throughout the region. Sales in Canada decreased 22% in Q2 and 15% year-to-date, due to the timing and decreased promotional level of activities and programs, as well as an unfavorable impact from changes in foreign currency exchange rates. At constant currency, sales in Canada would have declined by 15% in the second quarter.

Now on to the EMEA segment, which includes Europe, the Middle East, and Africa. Sales in the EMEA segment were up 16% in Q2, and are up 9% year-to-date, as compared to prior-year periods. Changes in foreign currency exchange rates had a favorable impact on sales in the second quarter.

On a constant currency basis, sales in the EMEA segment would have increased 13% in Q2. Changes in foreign currency exchange rates did not have a material impact on year-to-date sales. The segment accounted for 40% of global sales in Q2, compared to 38% in the prior fiscal year.

We sell into EMEA through a combination of direct operations in certain countries, as well as through exclusive marketing distributors in other countries. Sales in our EMEA direct markets were up 9% in Q2, and are up 3% year-to-date.

The sales growth in the second quarter was primarily due to promotional activities, and the increased sales of the WD-40 Specialist product line, stemming from new distribution and additional product offerings. Sales growth year-to-date was primarily due to new distribution, continued growth of the base business, and positive impacts of sales price increases. The direct markets accounted for 64% of EMEA's total sales in Q2, compared to 69% in the prior fiscal year period.

We sell through exclusive marketing distributors in Eastern and Northern Europe, and in the Middle East, India and Africa, with most of the sales consisting of the WD-40 brand. Our distributor markets in total were up 33% in Q2, and up 19% year-to-date.

The distributor markets accounted for 36% of EMEA's total sales in Q2, compared to 31% in the prior fiscal year period. We experienced double-digit sales across the distributor markets in Q2 and year-to-date, due to the continued growth of the base business in key markets, a successful promotional program in Russia, and the increased sales of the WD-40 Specialist product line in Eastern Europe.



Now, the Asia-Pacific segment. Sales in the Asia-Pacific segment were down 21% in Q2, and are down 8% year-to-date. Changes in foreign currency exchange rates had an unfavorable impact on sales in the second quarter, and year-to-date.

On a constant currency basis, sales in Asia-Pacific segment were down 16% in Q2, and down 4% year-to-date. The segment accounted for 12% of global sales in the second quarter, and 14% year-to-date.

Sales in Australia decreased 3% in Q2, and were down 1% year-to-date, compared to prior-year fiscal periods. Although reported sales decreased period to period, sales increased on a constant currency basis, due to the base business and the launch of the WD-40 Specialist product line in Q2.

Sales in China decreased 28% in the second quarter, and were down just 2% year-to-date. The sales decrease in the second quarter was attributed to differences in promotional activity, programs were more significant, and our customers purchased more products in the second quarter of fiscal 2003 (sic), as compared to programs in the current fiscal year. We also believe sales have been impacted by lower overall growth in the region.

Be reminded, we continue to focus on the long-term opportunities in China, but there will continue to be a lot of volatility along the way, due to the timing of promotional programs, the building of distribution, the shifting economic patterns, and the varying industrial activities.

Sales throughout the rest of Asia decreased 30% in Q2, and 15% year-to-date. The lower sales in the quarter were driven by a backlog of orders that we were unable to ship in Q2 of this fiscal year. We expect to ship these orders in Q3 of this fiscal year.

Sales were also impacted in Indonesia from the continuing transition to a new marketing distributor. That's it for the sales update.

Now I'll pass it over to Jay, who will continue with the review of the financials. Thanks, Jay.

Jay Rembolt - *WD-40 Company - CFO, Treasurer and VP of Finance*

Garry, thank you so much. Just a reminder, in addition to the information that we'll provide on this call today, we suggest that you review our Form 10-Q, which we'll file tomorrow.

Now let's first review our 50/30/20 rule, the measures that we use to guide our business. As you may recall, the 50 represents gross margin, which we target to be at or above 50% of net sales.

The 30 represents our cost of doing business, which is our total operating expenses, excluding depreciation and amortization. Our target is 30% or less.

And then finally, the 20 represents EBITDA. If our gross margin is at or above 50%, and our cost of business is 30% or less, our EBITDA will be at or above the 20% target.

EBITDA is earnings before interest, taxes, depreciation and amortization. The descriptions and reconciliations of these non-GAAP measures are available in our 10-Q, and in our investor presentations.

Now a look at gross margin or the 50. Gross margin in the second quarter was 51.6%, compared to 50.9% in the prior fiscal year period. The increase of 70 basis points in gross margin was primarily driven by lower input costs, as well as the impact of price increases implemented during the last 12 months, all of which were partially offset by higher promotional discounts.

A look at input costs, we experienced a net favorable impact of 70 basis points from our major input costs. This was driven by changes in the cost of petroleum-based materials, along with lower can costs in our Asia-Pacific and EMEA segments. The net impact of changes in other input costs was not material.



Sales price increases are considered and implemented on a country-by-country basis periodically, to help offset the impact from input cost increases. Period versus period, our gross margin improved by 30 basis points, as a result of price increases. This was offset by higher promotional discounts, which had an unfavorable impact on our gross margin of 30 basis points.

A higher percentage of sales during the current quarter was subject to promotional allowances, compared to that in the prior year. The cost of promotional activities, such as sales incentives, trade promotions, cash discounts that we give to our customers, are recorded as a reduction in sales.

The timing and magnitude of these activities cause fluctuations in gross margin period-to-period. All other impacts to gross margin, combined, were neutral for the quarter, and these include changes in foreign currency exchange rates in our EMEA segment, sales mix, manufacturing cost savings, and all other miscellaneous impacts. The themes discussed for the quarter for gross margin also apply to the year-to-date results.

Gross margin year-to-date was 51.8%, compared to the 50.5% in the prior fiscal year. The increase of 130 basis points in gross margin was primarily driven by the combination of price increases, lower promotional discounts, lower input costs, manufacturing cost savings, and a net favorable impact year-to-date from changes in foreign currency exchange rates in our EMEA segment. That completes our gross margin.

Now let's take a look at the 30, or our cost of doing business. In both the second quarter and our year-to-date period, the cost of doing business was 34%, compared to 33% in the prior fiscal year periods. While our goal is to have the cost of doing business at or below 30% of net sales, the percentage may fluctuate due to the changes in sales and timing of expenses, as well as investments that we make for the future.

Year-to-date, 69% of our cost of doing business came from three areas. 39% is related to people costs, or our investments in our tribe, 18% from our investments in marketing and advertising and promotional activities, and finally, 12% in freight costs, which is getting our product to our customers.

Now more details on our SG&A expenses. In Q2, they increased by 11% to \$26.7 million. As a percentage of net sales, SG&A expense was 28.3% in Q2, compared to 27.6% in the prior-year quarter.

Employee-related costs increased by \$1.2 million due to higher staffing levels, as well as higher compensation costs, associated with annual merit increases and higher bonus expense. Professional services, along with travel and meeting expense, were each up \$0.2 million. Freight expense was up \$0.4 million versus the prior period, due to higher sales volume, and all other miscellaneous expenses combined increased by \$0.6 million, and these include research and development costs, depreciation expenses, regulatory compliance costs, and others.

Changes in foreign currency exchange rates had an unfavorable impact period-to-period, increasing SG&A expenses by \$0.1 million. The themes discussed for the quarter also again apply to year-to-date results.

SG&A expense year-to-date was \$53.4 million, versus \$49.3 million in the prior fiscal year period. And as a percentage of net sales, it was 28.1% this fiscal year, versus 27.1% in the prior fiscal year.

Advertising and sales promotion expense increased by 14% in Q2 to \$6 million. As a percentage of sales, A&P investment was 6.4% in Q2, compared to the 6.1% in the prior-year period. The increase in advertising and sales promotion expense was primarily associated with the promotional programs conducted in the Americas this period.

Year-to-date advertising and sales promotion expense was \$11.6 million compared to \$11.3 million in the prior fiscal year period. Advertising and sales promotion expense, as a percentage of sales, decreased to 6.1% year-to-date, from the 6.2% in the prior year. The slight increase in advertising and sales promotion expense year-to-date was primarily driven by the aforementioned increase in the Americas programs during Q2.

Our amortization of intangible assets increased to \$0.7 million in Q2, compared to \$0.5 million in the prior-year period. And year-to-date amortization was \$1.2 million compared to \$0.9 million in the prior period. The increase in the year-to-date amortization was primarily due to the change in the useful life of the 2000 Flushes trade name in Q3 of the last fiscal year.



Total operating expenses in the current quarter were \$33.3 million, compared to \$29.7 million in Q2 of last year. Operating income in Q2 was \$15.3 million, compared to \$14.4 million in the prior-year quarter. And year-to-date total operating expenses were \$66.2 million, versus \$61.6 million in the prior-year period.

Operating income year-to-date was \$32 million, compared to \$30.3 million in the prior fiscal year. EBITDA, the last of our 50/30/20 measures, was 18% of net sales in Q2, compared to 19% in the prior-year quarter.

Year-to-date EBITDA was 18% to net sales in both the current and prior-year periods. Again, we target EBITDA to be at 20% but expect variations from time to time as sales, A&P investment and other expenses fluctuate with the timing of our activities, as well as our investments that we make for the future.

Interest income and interest expense remained constant in the second quarter, with net interest expense increasing by \$0.1 million year-to-date. Other net expense increased by \$0.8 million in the second quarter, and \$1 million year-to-date.

The change period-to-period was mainly due to fluctuations in exchange rates, primarily the Great British Pound against the Sterling -- or against the US dollar. We recorded foreign currency exchange losses in the current fiscal year compared to foreign currency exchanges in the prior fiscal year.

The provision for income tax in Q2 was 31%, versus 30.2% in the prior-year quarter. The higher tax rate in the current year is primarily driven by changes in the proportion of the Company's earnings which are foreign, and are taxed at lower rates. Year-to-date, the provision for income taxes is 30.6%, in both the current and prior fiscal year periods.

Net income in Q2 was \$11.3 million, versus \$10.5 million in the prior-year quarter. Change in foreign currency exchange rates period-to-period did not have a material impact on the translation of our results during the second quarter.

Diluted earnings per common share was \$0.67 in Q2, compared to \$0.66 in the prior fiscal quarter. Diluted shares outstanding decreased from 15.7 million shares to 15.3 million shares. And year-to-date, net income was \$21.8 million, versus \$21.4 million in the prior year.

Changes in foreign currency exchange rates had an unfavorable impact on the translation of our results by \$0.2 million. Our year-to-date results, translated at last year's exchange rates, or what we term as constant currency basis, would have produced net income of \$22 million versus the actual \$21.8 million.

Diluted earnings per common share were \$1.41 year-to-date, compared to \$1.35 in the prior fiscal year period. Diluted shares outstanding decreased from 15.7 million shares to 15.3 million shares.

A look at our balance sheet on February 28. Our balance sheet continues to remain strong, as cash and term deposits continue exceeding our debt.

At February 28, our cash and cash equivalents were \$41 million, and we had \$45 million in short-term investments, consisting of term deposits and callable time deposits, held in money center banks. The current portion of our debt under our existing line of credit was \$73 million, represented a \$10 million increase in the line during the second quarter, and was primarily used for the repurchase of our shares.

We continue to return capital to our shareholders through regular dividends and share repurchases. Regarding the dividend, on March 25th, the Board of Directors declared a quarterly cash dividend of \$0.34 a share, payable on April 30 to shareholders of record on April 11, 2014. Based on today's closing price of \$77.82, the annualized dividend yield would be 1.75%.

As for share repurchases, we acquired nearly 240,000 shares of our stock, at a total cost of \$17 million during the second quarter. These shares were acquired under our latest share repurchase plan, approved by the Board of Directors in June of 2013.



It provides authorization to acquire up to \$60 million of the Company's outstanding shares through the plan's end date of August 2015. We expect to continue executing our share repurchase program throughout the remainder of the year.

Well, that completes our financial review. Again, more information will be available on our 10-Q we'll be filing tomorrow, and now back to Garry.

Garry Ridge - *WD-40 Company - President and CEO*

Thanks, Jay. Looking forward, we remain cautiously optimistic about several macroeconomic factors. As per our second quarter and year-to-date results, we expect that growth in EMEA and the Americas will continue to more than offset any lower industrial activity and sales in Asia-Pacific.

We also hope there will continue to be a relative stability in input costs, and that our efforts to improve operations and sourcing will benefit our gross margin. We also expect the benefit we currently have in our margin will help offset unfavorable impacts we are beginning to see, related to changes in foreign currency exchange rates.

Given this outlook, our guidance remains unchanged from what we shared with you in January. The following fiscal year 2014 (sic) guidance does not include any acquisitions or divestiture activity, and assumes that foreign currency exchange rates will remain close to recent levels. We expect our fiscal year net sales results to be in the range of \$383 million to \$398 million, or a growth of between 4% and 8% versus fiscal 2013.

We project gross margin to be close to 51%. We expect our global advertising and promotional investment to be in the 6.5% to 7.5% of net sales. We expect income of \$40.5 million to \$42.8 million, which would achieve our diluted EPS of \$2.65 to \$2.80, assuming 15.3 million weighted average shares outstanding.

So in summary, what did you hear from us in today's call? You heard we increased sales by 8% in the second quarter, and that double-digit growth in the Americas and EMEA more than offset lower activity in our Asia-Pacific region. You heard we doubled sales of our Specialist product line, and that we launched new offerings in Europe.

You heard that we grew gross margin by 70 basis points over the period, and that we continue to be above our target. You heard that we continue to make progress on and benefit from our strategic initiatives, including new SKU launches to grow sales, our aerosol can project to reduce costs, and programs to increase margins.

You heard that we grew diluted earnings per share to \$0.67 in the second quarter, and returned capital to shareholders through the purchase of 239,501 shares, at a cost of \$17 million. You heard that our outlook is cautiously optimistic, and that we are maintaining our guidance with sales growth of 4% to 8% for fiscal year 2014.

In closing, I'd like to share a quote with you from Franklin D Roosevelt: The only limit to our realization of tomorrow will be our doubts of today. Let us move forward with strong and active faith.

Thank you for joining us today. We would be pleased to now open the conference call to your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

We'll go first to Liam Burke with Janney Capital Markets.



Liam Burke - *Janney Montgomery Scott - Analyst*

Garry, you said that Eastern -- or the distribution side of the European business was up 33%. A lot of those are smaller or more emerging markets. Do you see any similarities between those markets and the ones that you serve that are more -- relatively more developed, like China?

Garry Ridge - *WD-40 Company - President and CEO*

Well, there are a couple of big markets in that Eastern bloc as well, Liam, places like Poland and Russia are in that bloc. So I think overall in Eastern Europe, we continue to see an increase of people being aware, and using more of our blue and yellow can, plus we've been pleased with the adoption of our Specialist product line in a number of countries, including Russia, which was one of the first of those distributor markets to take on a range of Specialist earlier in the year.

Liam Burke - *Janney Montgomery Scott - Analyst*

Now, do you see any conflict between a newer WD-40 introduction and Specialist, or do you see them growing together?

Garry Ridge - *WD-40 Company - President and CEO*

We don't take Specialist into a market until the WD-40 core brand has a measured level of awareness and acceptance. We have to have that to get buy-in, or to gain from leveraging what we call the power of the shield.

But it's not unlikely that both could grow at similar rates in the initial period. Again, we believe, and still believe, the blue and yellow can market is bigger than the Specialist market. But we may be learning that to be different in some places over time.

Liam Burke - *Janney Montgomery Scott - Analyst*

Okay. And then on China, you spoke about how you had some cost savings on aerosol cans. Is that production facility meeting your expectations, and has it been running up to how you thought it would?

Garry Ridge - *WD-40 Company - President and CEO*

Yes, absolutely. It's delivered as we want, and is well-placed to deliver the volumes that we need in the foreseeable future.

Liam Burke - *Janney Montgomery Scott - Analyst*

Thank you, Garry.

Operator

And we will go next to Ben Richardson with JPMorgan.

Ben Richardson - *JPMorgan - Analyst*

Just a quick question about the ERP implementation in Europe. Just any idea about possible savings, and the timing of that implementation?

Garry Ridge - *WD-40 Company - President and CEO*

We're in the final pilot program. We expect to -- we will progressively implement it in different geographic areas over a year.

Most of the -- all of the initial costs have been sunk costs, so we would think that it will be at least a year from now until it's fully operational, in all of the geographies of Europe. It's more providing capacity than cost savings. As our business has grown substantially over there, we've needed more capacity to be able to facilitate the transactions.

So it's more really -- there are obviously efficiencies, but we don't think that it's going to reduce the number of people we have. In fact, we've probably increased a couple. So it's preparing us for the future growth.

Ben Richardson - *JPMorgan - Analyst*

Okay. And then on the topic of share repurchase, it seems that you're going at a pretty good clip here. What remains of the \$60 million, and you mentioned that you'll likely consider to buy -- execute that throughout the year, but what might be the pace of that?

Jay Rembolt - *WD-40 Company - CFO, Treasurer and VP of Finance*

Well, we've targeted somewhere between \$30 million to \$35 million on an annual basis, and that would effectively take us up through a couple months prior to our current authorization.

Ben Richardson - *JPMorgan - Analyst*

Okay. And what remains at this point?

Jay Rembolt - *WD-40 Company - CFO, Treasurer and VP of Finance*

\$35 million.

Ben Richardson - *JPMorgan - Analyst*

\$35 million. Okay. Perfect.

Jay Rembolt - *WD-40 Company - CFO, Treasurer and VP of Finance*

Right.

Ben Richardson - *JPMorgan - Analyst*

Outstanding. Thank you.

Operator

We'll go next to Joe Altobello with Oppenheimer.



Joe Altobello - *Oppenheimer & Co. - Analyst*

A couple quick questions, I guess on Asia-Pacific, first. In terms of the weakness this quarter, you mentioned that there was a backlog of orders that were supposed to ship in the first quarter, got pushed back into the second.

Could you quantify for us -- actually, from the second into the third. Could you quantify how much of those orders got pushed back?

Garry Ridge - *WD-40 Company - President and CEO*

We probably would have been reasonably flat, if they would have shipped for the quarter. And they're all to distributor markets, so they're all -- there was orders that were going to places other than Australia and China, where we manufacture, but they're all distributor business.

Joe Altobello - *Oppenheimer & Co. - Analyst*

Okay. And the way you described it, it sound like those orders have not been shipped yet, as of April 8?

Jay Rembolt - *WD-40 Company - CFO, Treasurer and VP of Finance*

Yes, they've shipped.

Joe Altobello - *Oppenheimer & Co. - Analyst*

Okay. They have. They have. And China, could you tell us what China did in the quarter, year-over-year?

Garry Ridge - *WD-40 Company - President and CEO*

I think we mentioned it. I think --

Joe Altobello - *Oppenheimer & Co. - Analyst*

I apologize.

Garry Ridge - *WD-40 Company - President and CEO*

You got another question while we find that?

Joe Altobello - *Oppenheimer & Co. - Analyst*

In terms of gross margin, I think year-to-date you've done 51.8% or thereabouts. Your guidance is still around 51%.

So maybe I'm reading this too literally, but that would imply some decline both sequentially as well as year-over-year. So help us understand why we would see the decline in gross margin that you guys are guiding to in the back half of the year.



Garry Ridge - *WD-40 Company - President and CEO*

We're not that good at forecasting the future. He who guides by the crystal ball gets to eat glass.

So there's nothing significant there, but we've got exchange rates, we've got volatility in oil prices, all of the normal things. I think as you might have gathered from the call, we were potentially reasonably comfortable that we're going to be at least at where we're guiding. Jay, you had a --

Jay Rembolt - *WD-40 Company - CFO, Treasurer and VP of Finance*

Essentially, we left guidance alone. We are very pleased that our margin is up over that 51%.

But we really are guiding toward the -- our bottom line earnings, and we have left it alone. We feel fairly comfortable in that range.

Joe Altobello - *Oppenheimer & Co. - Analyst*

Okay. And then in terms of Specialist, obviously you mentioned that it doubled year-over-year, a lot of that coming from new distribution, I think Australia was part of that new distribution. Where are there other big markets that you still have to go into with that brand, over the next 6 to 12 months or so?

Garry Ridge - *WD-40 Company - President and CEO*

There's a number of aspects to that, Joe. Firstly is, it's not only the brand but it's the categories that we choose to go into.

So we're not only increasing distribution of Specialist, but in the United States, for example, we're still at early days. We continue to get more of the SKUs of the different categories into distribution. They're delivering excellent results for our retailers.

We're actually growing categories that were not growing before, so our retailers are very comfortable with that. Specialist is a long, long road, and we'll be talking about it for as long as I'm here, and probably longer than that. So we believe that it is what we expected it would be, which is our platform for leveraging the power of the shield.

We're certainly delighted that we've doubled sales year-over-year. It's becoming a significant number now, and now that we've seen that performance, we gain more confidence about our ability to be able to very deliberately extend the brand.

And I say the word deliberately, because this is not a -- just slap that shield on anything. There's a lot of work been going on over the past many years, and consistently, and into the future about where we'll take it.

So, the world as you know is our oyster. We can take things to more people, in more places, faster than anyone else, now.

We spent the last 10 years building up that distribution center globally and I think Specialist really shows how having set up that distribution, we are able to take more things, to more people, in more places, faster. So Specialist is a very -- we're in a comfortable position with this, and we feel good about the future.

Joe Altobello - *Oppenheimer & Co. - Analyst*

Okay. Thanks, Garry. Thanks, Jay.



Operator

We'll go next to Linda Bolton Weiser with B. Riley.

Linda Bolton Weiser - *B. Riley & Co. - Analyst*

First, can I just ask for a clarification on what you said on Asia. Did you mean that the whole Asia-Pacific segment would have been flat, excluding the back order issue, or just the rest of Asia-P so it was down 30%?

Garry Ridge - *WD-40 Company - President and CEO*

The rest of Asia. Well, when you look at -- Australia was relatively flat, anyhow. China was down, and the rest of Asia would have been flat, if we would have shipped that backlog.

Linda Bolton Weiser - *B. Riley & Co. - Analyst*

Okay. I got you. And then did you see -- well, just on that issue with the Indonesia distributor transition, I can't quite remember how long you've been talking about that, but when did that issue start to impact, and when will we fully anniversary that disruption from that?

Garry Ridge - *WD-40 Company - President and CEO*

We changed the distributor in September last year, so we will lap it this September, and what we're going through really is a ramp-up with the new distributor. So it took time to ship product into our new distributor. There was a, if you will, a bit of a gap in the market.

But in-market sales are good and that's -- it's just an event. It's not a trend. We'll be through it, and on our way.

Linda Bolton Weiser - *B. Riley & Co. - Analyst*

Okay. And then I was wondering in -- did you see any uptick in consumption demand in Philippines because of clean-up efforts there after the typhoon, and how does Philippines rank in terms of size of market for you? Is it one of the smaller, or how does it rank versus India and a few of those other markets there?

Garry Ridge - *WD-40 Company - President and CEO*

It would be a mid-sized market, as far as consumption is concerned in Asia-Pacific. India would be smaller than the Philippines, because India is not as developed yet.

We may have seen some, but I think as we've talked before, Linda, it would be very unusual to see a needle move because of a particular geographic climatic condition, that would be so obvious, amongst the scheme of things. We always see an uptick in consumption, but it's event-driven, and it's just an opportunistic result. It normally doesn't make a huge difference.

One of the reasons also is that the events happen and sometimes -- and the product has to get to that region. They don't carry excess inventory, hoping for a typhoon. So we may see some depletion of inventory and some top-up later, but it's really hard to be able to focus in on one geographic area, particularly a country the size of Philippines, and think that it might make a difference.



Linda Bolton Weiser - *B. Riley & Co. - Analyst*

Okay. And then can you just talk -- I think your normal habit is to redo some tin contracts in January. Can you give us some rough idea how that went?

Does that kind of bake in a lower tin cost, moderately lower, or much lower, flat? Can you give some color on that?

And also, it seems like petroleum-based costs might be down a little bit since you last reported. Would that be true? Thanks.

Jay Rembolt - *WD-40 Company - CFO, Treasurer and VP of Finance*

Actually, today they're -- in the last few days, they've been up. There around \$100 -- little over \$100. Where I think we last reported we were more in the \$90s I think.

But from a standpoint of the tin plate in our contracts, yes, we did -- in the US, we renegotiated our contract in the first quarter or in the first part of the year, January. And essentially we saw no increase in the pricing this year. We had some negotiations that lowered our can costs at the very end of last year, and so we are going into this year with lower can costs.

Linda Bolton Weiser - *B. Riley & Co. - Analyst*

Great. And just one last thing. Did you say that the other expense item was more negative than in prior-year, because primarily of FX? Was that the reason?

Jay Rembolt - *WD-40 Company - CFO, Treasurer and VP of Finance*

Yes, yes, yes. We had gains on foreign currency transactions in the prior year, whereas this year we had some foreign currency exchange losses.

Linda Bolton Weiser - *B. Riley & Co. - Analyst*

Okay. Great. Thanks a lot.

Operator

We'll go next to Rosemarie Morbelli with Gabelli & Company.

Rosemarie Morbelli - *Gabelli & Company - Analyst*

I was wondering if you could talk about what you are seeing in terms of overall demand in Europe. Have you seen an uptick, as many companies have seen? Or are your products not as affected by the economic turnaround that we expect?

Garry Ridge - *WD-40 Company - President and CEO*

Well, I think you'll see that when -- last year, when Europe went through its economic challenges, was it last year? I think it was, or the year before, we also went sideways, not necessarily because of a lack of demand of our product, but more as a result of activities of the retailers and distributors who sell our product. We've seen a steady increase in confidence over the past 18 months in Europe, and that's been reflected in the sort of results that you're seeing being delivered now.



So, we're very encouraged about our opportunities for a long period of time into Europe. We'll weather the storms as they come, and our product itself, again, is not necessarily that impacted by the end user. It's more impacted by the activities of the distributors and wholesalers.

Rosemarie Morbelli - *Gabelli & Company - Analyst*

So when you look at what the activities of the distributors are, and if you look sequentially on a monthly basis, are you seeing since the beginning of the year, are you seeing sequential improvement every month, or it just doesn't work like that for you?

Garry Ridge - *WD-40 Company - President and CEO*

It doesn't work. We would have trouble over the many European countries that we're in, tracking them month-by-month. Quarter-by-quarter would be the best, but year-on-year, but we've seen a general increase in business activity across most of the European markets.

Particularly, one is Spain, Spain is doing reasonably well right now. It was one of the worst-performing markets 18 months ago. But our business in Spain has rebounded very significantly in the last year.

Rosemarie Morbelli - *Gabelli & Company - Analyst*

All right. That is very helpful, thank you. And I was wondering also if your sales in the US were affected by the bad weather we had, or if that has no impact whatsoever.

Garry Ridge - *WD-40 Company - President and CEO*

I can't say it has no impact but we certainly -- if it was any impact, I think it might have been reflected in the sales. We had a good quarter.

Certainly if customers can't get to stores to buy product, then we're not going to sell product. But we know that overall, the conditions will be impacted like most others, but there's nothing that we can say, this did that.

Rosemarie Morbelli - *Gabelli & Company - Analyst*

Okay. And then lastly, if I may. Could you talk about whether the turmoil in Russia and Eastern Europe is affecting your revenues, and whether you expect it to?

Garry Ridge - *WD-40 Company - President and CEO*

Not that we can see at this time. Whether it will or not, I'm not -- I don't know.

Rosemarie Morbelli - *Gabelli & Company - Analyst*

Okay. Thank you.

Operator

We have no further questions at this time. So I turn the conference back over to Garry Ridge, for any additional or closing remarks.



Garry Ridge - *WD-40 Company - President and CEO*

Thank you so much. Thanks for all of those who have joined us. Thanks for the questions, and we'll look forward to talking to you again on July 9.

Until then, keep spraying. Bye for now.

Operator

That does conclude today's conference. We thank you for your participation.

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