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WDFC - Q1 2014 WD-40 Company Earnings Conference Call

EVENT DATE/TIME: JANUARY 08, 2014 / 10:00PM GMT



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

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**Liam Burke** *Janney Montgomery Scott - Analyst*

**Yoyo Yen** *JPMorgan - Analyst*

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

## PRESENTATION

### Operator

Good day and welcome to this WD-40 Company first-quarter 2014 earnings release conference call. Today's call is being recorded.

At this time, I would like to turn the call over to President and Chief Executive Officer for WD-40 Company, Mr. Garry Ridge. Please go ahead, sir.

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

Good day. Before we start, I'd like to remind you that except for the historical information, this conference call may contain forward-looking statements concerning WD-40 Company'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 -- statements including the impact of commodity prices, the introduction of new product lines, and the fluctuating global market conditions, including foreign currency exchange rates, and both impacting 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 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.WD40.com](http://www.WD40.com).

Thanks for joining us today on the conference call, and we'd like to go now and discuss the first-quarter results. Today, we reported net sales of \$95.5 million for the first quarter of fiscal 2014, which was slightly above Q1 of last year, and was a record quarter for the Company. Net income for the first quarter was \$11.5 million compared to \$10.9 million in Q1 of last fiscal year. Diluted earnings per share for the first quarter was \$0.74 compared to \$0.69 for the same period last fiscal year.

As we review our results for the first quarter, we'll be doing so under our 50/30/20 rule and our strategic initiatives. While global sales remain fairly flat due to the timing of promotional activities, we increased our gross margin to 52%, partly attributed to our strategic initiatives. We also prepared for many opportunities and challenges in fiscal year 2014. Before we dive into the financials, I'd like to take a moment to update you on our refreshed strategic initiatives.

Strategic initiative number one is to grow the WD-40 multiuse products. We had a moderate sales increase in WD-40 multiuse product in the first quarter of Q1 compared to last fiscal year. This growth was lower than average, due to the timing of promotional activities year-over-year. We had strong promotional activity in the first quarter last year, whereas we did not have that in the current quarter in most markets. We also had a lower level of replenishment orders after the exceptionally strong fourth-quarter promotional efforts in fiscal 2013.



We did nevertheless experience double-digit growth in several markets within our European segment, which we now refer to as EMEA. EMEA includes Europe, Middle East, Africa, and India. We also experienced double-digit growth in China and many distributor markets in the Asian region. Furthermore, we sold into Albania for the first time, bringing WD-40's brands' global reach to 188 countries.

Strategic driver number two, which is to grow the WD-40 Specialist product line. The WD-40 Specialist product line continued to support the brand with double-digit growth in Q1 compared to the prior-year first quarter. We launched the product line into eight new countries in Q1, including Australia and Turkey, and smaller countries in Eastern Europe, the Middle East, and the Caribbean. We also continued working on new formulations and delivery systems for the future WD-40 Specialist products.

Strategic initiative number 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 multiuse products and Specialist product lines. Over the last few years, we have launched several new SKUs within our existing portfolio of brands, including WD-40 Bike, 3-IN-ONE, and our household and cleaning products. Additional SKU launches are planned for fiscal year 2014, particularly in our 3-IN-ONE brand.

Strategic driver number four is to develop and retain and attract outstanding tribe members. Developing our tribe members is of utmost importance to us. We mentioned to you last fiscal year that we launched the Tribology University, a program on technical product knowledge that enables our tribe to better converse about the attributes and features of our fine products. Our initial pilot in the US went very well, and we are now taking the concept to the next level with eLearning side courses, exams, and with programs for our global tribe members. All tribe members from sales to accounting will have the opportunity to better learn about our products and position themselves for greater opportunity with our customers within the Company.

Strategic driver number four is operational excellence. We put tremendous effort into the operational excellence of our company. So, it was only natural to have this initiative out on its own. This includes continuous improvement by optimizing resources, systems, and processes. This is important in managing our time/talent/treasure and our technology as we scale up our business. Operational excellence is also key to achieving an ever-increasing customer and regulatory requirements, as well as helping to offset costs to protect our gross margin and profitability.

We have several recent examples of operational improvements and excellence, including our local sourcing initiative in China, third package of consolidation in the Americas, aerosol can sourcing project in China and Europe, and a strong track record of shipping orders on-time in-full. We have several projects planned for 2014. First, we'll be focusing on achieving new regulatory requirements, including a smooth transition to a lower VOC formulation in California.

Second, we will continue our can-sourcing project, with focus on the Americas, as well as improving operational efficiency within our supply chain network.

Third, we are investing in systems to improve our back office operations, including a major upgrade of our ERP system in EMEA, and a new global human resource information system. That completes the update of our strategic initiatives, so let's move on to the details of our first quarter's results, starting with sales.

Sales grew \$300,000 period-versus-period, as growth from multipurpose maintenance products more than offset declines in our homecare and cleaning products globally. We had a modest growth in Asia-Pacific, which impact -- was impacted by the timing of promotions and shipments year-over-year. This includes sales that shipped at the end of fiscal 2003 that were planned for Q1 of fiscal 2004. The prior-year first quarter was also one of the best on record, due to the high replenishment orders in EMEA, and a higher level of promotional activity, as well as new distribution of WD-40 Specialist product line.

Markets outside the US accounted for 63% of global sales in Q1 versus 62% in the prior-year period. Sales are, in the multipurpose maintenance products category, accounted for 88% of global sales compared to 86% in the prior-year period. Our multipurpose maintenance products sales were up 3% in Q1 compared to the prior fiscal-year quarter. By trading bloc, the category was up 1% in the Americas, up 4% in EMEA, and up 6% in Asia-Pacific. Global WD-40 brand sales grew by 3% in Q1 compared to the prior fiscal-year quarter. This was driven by sales growth in both our WD-40 multiuse product -- the familiar blue and yellow can -- and the WD-40 Specialist product line in EMEA and Asia-Pacific.



Homecare and cleaning product sales continue to represent a smaller portion of our business per our strategic road map. The category accounted for 12% of global net sales in Q1 compared to 14% in the prior-year period. These products include Spot Shot, 2000 Flushes, Carpet Fresh, No Vac, 1001, X-14, and the Lava and Solvol brands. Total homecare and cleaning products sales were down 15% globally in Q1. By trading bloc, sales in homecare and cleaning products were down 16% in the Americas, down 14% in EMEA, and down 8% in Asia-Pacific. Decreased sales of homecare and cleaning products in the Americas was mostly attributed to Carpet Fresh, Spot Shot, and 2000 Flushes automatic toilet bowl cleaners, which were down 51%, 21%, and 7%, respectively.

These brands were impacted by some lost distribution that occurred mid-fiscal-year 2003, particularly in the warehouse channel, as well as decreased promotional programs and category declines. 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 business in low-margin products, and programs which require significant trade discounts.

Lower homecare and cleaning product sales in EMEA are partly due to the timing of promotional activities year-over-year. Replenishment sales of the 1001 brand were particularly strong in the prior-year period; lower sales of homecare and cleaning products in Asia-Pacific primarily due to the unfavorable impact from the change in foreign currency exchange rates. We continue to evaluate strategic alternatives for certain of the Company's homecare and cleaning products during the first quarter, but no decision has been made to date to change the strategic plans for these brands.

Now we'll talk a little more about our results by segment. Let's start with the Americas. Sales in the Americas decreased to \$44 million in Q1 or 3% versus Q1 of last fiscal year. The segment accounted for 46% of global sales in Q1 and 48% in the prior-year period. Total sales in the US were down 3%, with the aforementioned declines in homecare and cleaning products more than offset modest growth in our multipurpose maintenance products sales. Sales in Latin America, which are mostly the three -- the WD-40 brand, remain flat period-versus-period. Sales in Canada decreased 6% in the first quarter, primarily due to lower sales of Spot Shot and the WD-40 brand, but as well as unfavorable impact from changes in foreign currency exchange rates.

Moving on to our EMEA segment, sales in the EMEA segment, which includes Europe, the Middle East, Africa, and India, increased to \$36.5 million in Q1, up 3% versus Q1 of last fiscal year. This segment accounted for 38% of global sales compared to 37% in Q1 of last fiscal year. Changes in foreign currency exchange rates period-versus-period did not have a material impact on sales. We sell into EMEA through a combination of both direct operations in certain countries as well as through exclusive marketing distributors and others.

Sales in our EMEA direct markets were down 2% in Q1. The decrease period-versus-period is mostly attributed to the timing of promotional activities, as the region had a strong promotional activities in the fourth quarter of fiscal 2013. The prior-year period also had a high level of replenishment orders. We sell through exclusive market -- independent marketing distributors in Eastern and Northern Europe, India, Africa, and in the Middle East, with virtually all these sales consisting of the WD-40 brand. Our distributor markets were, in total, up 10% in Q1 due to promotional activity and the continued growth of the WD-40 multiuse product. The distributor markets accounted for 44% of EMEA sales in Q1 compared to 41% in the prior fiscal-year period.

Now we'll look a little more at Asia-Pacific. Sales in Asia-Pacific, which includes Australia, China, and other countries in the Asian region, increased to \$15 million in Q1 or 4% versus Q1 of last fiscal year. The segment accounted for 16% of global sales in Q1 versus 15% in the prior fiscal-year period. Changes in foreign currency exchange rates had an unfavorable impact on sales. On a constant currency basis, sales would've been \$15.4 million with an 8% growth over the prior-year period.

Sales in Australia remain constant at \$4.6 million in Q1. Changes in foreign currency exchange rates had an unfavorable impact on sales. And on a constant currency basis, sales would have increased \$600,000 or 13%. The growth on a constant currency basis was due to the launch of the WD-40 Specialist product line and increased promotional activities.

Sales in China increased 24% in Q1 to \$3.4 million, driven by both organic growth and the timing of promotional activities. We had a low level of promotional activity in the prior-year quarter compared to a relatively strong promotional activity in the current quarter. 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, shifting economic patterns, and the varying industrial activities.



Sales in the rest of Asia remained flat at \$6.9 million for the first quarter. Lower sales in Indonesia offset the sales growth in other distributor markets. The lower sales in Indonesia were due to the transition that we have been going through to a new marketing distributor.

That's it for me for now for the sales update. I will now pass over to Jay who will continue to review the financials.

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

Thanks, Garry. In addition to the information that we are presenting on this call today, we suggest that you review our Form 10-Q, which we'll be filing tomorrow. First, let's review our 50/30/20 rule -- that's the measures that we use to guide our business. As you may recall, the 50 represents gross margin. We target our gross margin to be at or above 50% of sales. The 30 represents our cost of doing business, which is our total operating expenses, excluding depreciation and amortization. Our target for that is 30% or less. And 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%.

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

First, let's take a look at the 50, or the gross margin. Gross margin in the first quarter was 52% compared to 50.1% in the prior fiscal-year period. The increase of 190 basis points in gross margin was primarily driven by price increases, lower promotional discounts, as well as lower input costs and lower manufacturing costs stemming from our supply chain-related initiatives. Our margin was also favorably impacted by changes in foreign currency exchange rates.

A quick look at the input costs. We experienced a favorable net impact of 30 basis points from our major input costs. Impacts from changes in the cost of petroleum-based materials and aerosol cans combined to favorably impact our gross margin by 50 basis points. Much of this benefit came from the Asia-Pacific and EMEA segments. Changes in our other input costs, including raw materials related to homecare and cleaning products, had an unfavorable impact of 20 basis points. Sales price increases are considered and implemented periodically on a country-by-country basis to offset the impact from cost increases. And, during this period, our gross margin improved 40 basis points as a result of price increases implemented during the prior fiscal year.

Lower promotional discounts had a positive impact on our gross margin of 70 basis points. Lower percentage of sales during the current quarter was subject to promotional allowances compared to that in the prior quarter. This was partially a result of lower sales of our homecare and cleaning products in the Americas, as well as lower promotional discounts being given on these products. The cost of promotional activities such as sales incentives, trade promotions, cash discounts that we give to customers are recorded as a reduction to sales, and the timing and magnitude of these can cause fluctuations in our gross margin period-to-period.

Looking at the changes as a result of our manufacturing costs, we achieved lower manufacturing costs in China and in the Americas. And we've been increasing the portion of our goods manufactured in China for the local market, since we began local production in the latter half of 2012. The higher proportion of goods manufactured in China positively impacted our margin by 10 basis points period-versus-period. In the Americas, we benefited from lower manufacturing costs stemming from the North American supply chain architecture project. The lower cost positively impact -- these lower costs positively impacted our gross margin by 20 basis points. Other impacts to gross margin include foreign currency exchange rates within our EMEA segment, which positively impacted our gross margin by 50 basis points.

Cost of goods are sourced in pounds sterling, while revenues are generated in euros, sterling, and the US dollar. The value of the euro increased period-versus-period causing revenues from euro-based countries to be worth more in pounds sterling, thus improving the gross margin of that region. Sales mix and all other miscellaneous impacts combined unfavorably impacted our gross margin by 30 basis points.

That completes the gross margin discussion. Now let's take a look at the 30 or our cost of doing business. Our cost of doing business was 33% in both Q1 of this year and the same period last year. In the first quarter, approximately 68% of the cost of doing business came from three areas -- 38% related to our people, the investments we make in our tribe; 18% from investments we make in marketing, advertising and promotion; and 12% is the cost of -- associated with the freight to get our products to our customers.



A little bit more details of our SG&A expenses. The SG&A expense in Q1 increased by 5% to \$26.7 million. As a percentage of net sales, it was 27.9% in Q1 compared to 26.6% in the prior-year quarter. We had higher employee costs of \$1.4 million due to higher compensation costs associated with annual merit increases, higher staffing levels. In addition, we had our -- in addition, both professional services and travel and meeting expenses were each up \$0.2 million, and were -- but were partially offset by lower freight expense, which was down \$0.3 million versus the prior period. All other miscellaneous expenses combined increased by \$0.3 million.

Changes in foreign currency exchange rates had a positive impact decreasing SG&A expenses by \$2 million -- by \$0.2 million, excuse me. Advertising and sales promotion expense decreased by 7% in Q1 to \$5.6 million. As a percentage of sales, A&P investment was 5.9% in Q1 compared to 6.4% in the prior-year period. The decrease in advertising and sales promotion expense was primarily due to lower costs associated with promotional programs conducted in the Americas, and the timing of promotional activities in the EMEA region.

Amortization of intangible assets remained relatively constant at \$0.6 million in Q1 compared to \$0.5 million in the prior-year period. Total operating expenses in the current quarter were \$32.9 million versus \$31.9 million in Q1 of last fiscal year. Operating income in Q1 was \$16.8 million compared to \$15.9 million in the prior-year quarter. EBITDA, the last of our 50/30/20 measures, was 19% of net sales in Q1 compared to 18% in the prior fiscal-year quarter. Period-versus-period, higher gross margin more than offset the higher operating expense, enabling us to grow our EBITDA percentage. As you know, we target EBITDA to be 20% of net sales, but expect variations from time to time, as sales, A&P investment, and other expenses fluctuate with the timing of our activities. Our EBITDA percentage is also affected by investments we continue to be making for future growth.

The provision for income taxes in Q1 was 30.3% versus 31% in the prior-fiscal quarter. The lower tax rate in the current quarter is primarily driven by the increasing proportion of the Company's earnings, which are foreign and are taxed at lower rates, along with tax provision adjustments associated with filing the Company's tax returns.

Net income in Q1 was \$11.5 million versus \$10.9 million in the prior-year quarter. Changes in foreign currency exchange rates did not have a material impact on net income. Diluted earnings per common share were \$0.74 in Q1 compared to \$0.69 in the prior fiscal-year quarter. Diluted shares outstanding decreased from 15.8 million shares to 15.4 million shares.

A look at our balance sheet at November 30; it remains -- continues to remain strong, as our cash and term deposits exceed our debt. At November 30, our cash and cash equivalents were \$51.4 million, and we had \$40.7 million in short-term investments, which consist of term deposits and callable time deposits held in money center banks. The outstanding balance of our debt under the current existing line of credit remains unchanged at \$63 million.

In addition to investing for future growth, we also focus on returning capital to our shareholders. First, we provide our shareholders with a regular dividend, which we targeted 50% of net income. On December 10, the Board of Directors declared a 10% increase in the quarterly cash dividend, increasing the dividend from \$0.31 per share to \$0.34 per share. The dividend will be payable on January 31, 2014, to shareholders of record on January 6, 2014. And based on today's closing price of \$75.55, the annualized dividend yield would be 1.8%. This is the fourth consecutive year of dividend increases.

We also have been returning capital to our shareholders through share repurchases. During the first quarter, we acquired approximately 78,000 shares of our stock at a cost of \$5.2 million. These shares were acquired under the latest share repurchase plan approved by the Board of Directors in June of last year. It authorizes us 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 on our share repurchase program throughout the remainder of this fiscal year.

That concludes the financial overview. More information, again, will be available in our Form 10-Q, which we'll file tomorrow. And now back to Garry.



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

Thanks, Jay. We sum up -- there are several macroeconomic factors that impact our outlook as well as our progress towards our strategic initiatives. We are cautiously optimistic about several macroeconomic factors, which include the stability of the global economy, major input costs, and foreign currency exchange rates.

In terms of sales, we feel the growth of our multi- -- WD-40 multiuse product and the WD-40 Specialist product line will overcome the uncertainty that continues to linger across the globe. We also expect our multipurpose products to offset decreases in our homecare and cleaning products. As for input costs, we hope that our initiatives will help us maintain our margin and offset the volatility and uptrend we are seeing in petroleum-based materials.

Now, on to our guidance, which remains unchanged from what we shared with you in our October call and the annual shareholder meeting in December. The following fiscal year 2014 guidance does not include any acquisition or divestiture activities, and it does assume that foreign currency exchange rates will remain close to recent levels. For the year, we expect our fiscal year net sales to be in the range of \$383 million to \$398 million. And that would be a growth of between 4% and 8% versus fiscal 2013.

We project our gross margin will be close to 51%. We expect our global advertising and promotional investments to be in the range of 6.5% and 7.5% of net sales. And we expect our net income to range somewhere between \$40.5 million and \$42.8 million, which would achieve a diluted earnings per share of between \$2.65 and \$2.85(sic - see press release "\$2.65 to \$2.80") assuming 13 -- sorry, 15.3 million weighted average shares outstanding.

In summary, what did you hear from us in this call today? You heard that the growth in our multipurpose products more than offset decreases in homecare and cleaning products. You heard that we grew gross margin to 52%, partly due to lower import costs and lower manufacturing costs stemming from our supply chain initiatives. You heard that we continue to make progress on our strategic initiatives, including preparing for a lower VOC formula conversion in California, as well as developing new SKUs for launch later in fiscal year 2014 and 2015. You heard we grew diluted earnings per share from \$0.69 to \$0.74 per share, and have increased our regular quarterly dividend by 10% to \$0.34 per share. And you heard that our outlook is cautiously optimistic, and that we are maintaining our guidance with sales growth of between 4% and 8% for fiscal 2014.

In closing, I'd like to share a quote with you from Nelson Mandela. "It's better to lead from behind and to put others in front, especially when you celebrate victory when nice things occur. You take the front line when there is danger. Then people will appreciate your leadership."

Thank you for joining us today. We'd be very happy to open for questions.

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## QUESTIONS AND ANSWERS

**Operator**

(Operator Instructions) Liam Burke, Janney Capital.

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**Liam Burke** - *Janney Montgomery Scott - Analyst*

Garry, could we get an update on the Specialist brand rollout? Its earliest -- I mean the most -- the longest time it's been on the shelves is in the North American markets, and then you sort of rolled out to Asia-Pacific. But could we get an update on how that's going?

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

Yes. Thank you, Liam. I think we're currently in 27 countries. We took it out to some new ones in Australia, I think in Turkey in the first quarter. We continue to be cautiously and optimistic but pleased with the progress. We continue to see ongoing replenishment sales in the North American





market, particularly in the hardware home improvement and automotive category. We're happy with the work that's happened in the UK with the motorcycle, and we're now rolling that into a couple of new countries.

So, we continue to see that Specialist will offer us good opportunity to execute and to deliver growth on the back of the power of the shield in the core brand. So, it's still -- even though it's been a while, it's still very early days for us. There's a lot of work to do. But we feel good about it.

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**Liam Burke** - *Janney Montgomery Scott - Analyst*

Okay. Thank you, Garry. You mentioned an ERP upgrade in the European or EMEA now. Do you anticipate any kind of disruption based on the guidance that you've given?

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

No. We are -- we're really at the near end of the upgrade. It's just a matter -- it's been running parallel for a while. There's some more work to be done. We don't see any disruption at all at this time. It's been progressively tested through a number of the markets. Our first go-live launch is May 2014.

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**Liam Burke** - *Janney Montgomery Scott - Analyst*

Okay, great. And then, Jay, you had some heavy working capital needs. Is there anything unusual there? Or can we expect a fairly normal cash flow -- cash flow similar to what we've seen in past years?

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

Yes. We expect \$40-plus-million on an annual basis of kind of free cash flow.

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**Liam Burke** - *Janney Montgomery Scott - Analyst*

Great. Thanks, Jay.

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

Thanks, Liam.

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**Operator**

Jeff Zekauskas, JPMorgan.

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**Yoyo Yen** - *JPMorgan - Analyst*

Hi, this is [Yoyo Yen] for Jeff. Could you please specify on the raw material guidance regarding which raw materials or manufacturing costs do you expect to really go up, given that the annual guidance of gross margin is 51% versus 52% for this quarter?





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

Well, we don't see -- we see the current range of raw materials is what's embedded in our current outlook on margin. So, we have other impacts associated with mix that may have -- that are built into some of that 51%.

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

But as we say, we say we expect it to be close to 51%. We're not good enough to be 100% laser accurate. But we're certainly happy at the moment that it's above 51%.

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**Yoyo Yen** - *JPMorgan - Analyst*

Do you see the recent trend of higher HDPE price on a year-over-year basis have any negative impact on your gross margin for the next quarter?

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

You mean plastics?

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**Yoyo Yen** - *JPMorgan - Analyst*

Yes.

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

Plastics has a -- is a very -- the two biggest components in our raw material costs are petroleum and steel cans, which I think together make up, Jay, about --?

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

About 60% --

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

60%?

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

65%, yes.

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

We don't have a lot of plastic in our overall cost basis.

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**Yoyo Yen** - *JPMorgan - Analyst*

Okay, I see. And also, from a longer-term perspective, where do you expect your SG&A expense would be in terms of the total sales from a longer-term perspective in order to get the 30% target?

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

Yes, I mean, we see the 30% being achieved over time as we grow revenue. We don't see a reduction in our current SG&A expenses. We see them continuing to grow, but not growing at the rate of sales. And as sales will increase, we'll be able to see that -- we'll be able to get closer to the 30%.

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**Yoyo Yen** - *JPMorgan - Analyst*

So, over time, is there a target, say, five years or 10 years? Or we don't know yet?

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

Well, in our minds, we have a target. The five-year range is really probably the -- I think that's a reasonable range for that target.

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**Yoyo Yen** - *JPMorgan - Analyst*

Okay, thank you.

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**Operator**

Linda Bolton Weiser, B. Riley.

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

Can you -- I mean, clearly, this is your hardest sales growth comparison of the year, and you explained that it was the timing of promotional activity. And in the second quarter, it looks like you have a much easier comparison. So is it reasonable to assume that we'll see a little bit higher sales growth in the second quarter? And is there any way to quantify the effect the timing had on the sales growth in the quarter?

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

Thanks, Linda. We don't comment quarter-to-quarter. What we do believe is that our range for the year between 4% and 8% is still a worthy range. But there are both promotional and geographic mix that affect quarter-to-quarter. You're right -- we just had the biggest quarter in the Company's history compared to the second-biggest quarter in the Company's history, which was the first quarter of last year.

So, although there would be a desire for us to get more granular, we really are in a position where we'd like to stay within the annual target. And we'll -- we see that we'll be talking about that again at the end of the next quarter. So, that's kind of where we feel we are right now.

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

Okay. And then I think that you've talked in the past about entering into context or modifying your contracts for the tin cans in January. Is that something to come further -- later in the month? Is there anything you can talk about in terms of -- do you expect those costs to be down year-over-year? Or is there any color you can give on that process?



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

Yes, at the moment, we're not expecting them to be down, but we aren't expecting a very significant increase either -- we are not expecting a dramatic increase either. We're still in negotiations and we'll be able to comment once those are completed near the end of the month.

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

Great. And then in terms of your expansion in Specialist and these other lines -- a motorbike and bike line -- is that -- is there any way to quantify how much of your SG&A increase is due to the investments behind that? I know you had a subsidiary for the bike line that had two employees. Are you going to be adding -- are you adding more people? Is this what the SG&A increase is? Or is it more just regular operating day-to-day investments?

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

It's regular operating day-to-day investments. We are really leveraging primarily the infrastructure that we have in place. But you're seeing increases in -- for things like our continued deployment of people in China, which we would be doing whether we had Specialist or not. But there is really very, very little incremental extra overhead associated with the Specialist growth.

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

Okay. And then in terms of the just general economic outlook, are you seeing changes? Like how does Europe feel to you? Because we had seen some signs of improvement, and I guess some of your European business was quite good this quarter. But do you sense any change, any reversal and softening or sort of a little bit of improvement there?

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

No. We think it's steady where it was. I was interested this morning on CNBC. They were talking about retail sales were up in Europe over the Christmas period. I think my view on Europe is there's less fear there now than there was a year ago. And fear is a paralyzing aspect. So, from our point, we feel steady as she goes. We feel reasonable about the European market, as we do everywhere right now. I think we're in a state of -- particularly in the segments that we operate in, where primarily housing and automotive seem to be doing okay. So, that's why we said we're cautiously optimistic about the macroeconomic conditions that are -- seem to be around us at the moment.

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

Okay. And I guess finally just on the lawn and garden line that you've alluded to in the past, is there anything else you can tell us? I mean I would think you would have to launch that, if you were going to, before the spring. Would that have to be by February or March? Or do you have anything you can tell?

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

Well, lawn and garden was an example of one of the things that we're working on. And we shared it as saying -- this is an area that we may go into. Where -- there are a number of those projects, in fact, on the table and we have to get the business model right for them. But we have a lot of work to do with Specialist still in other areas before we bring new categories in. But what we're really sharing is that we see that there are a lot of categories that Specialist has a potential to go in. We've been doing work around the opportunity in lawn and garden. We're looking at others, as I said. So, as we get closer and when we're ready to go, we'll either let you know that we're testing or piloting or we're going to go full stream.



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

Okay. And then can I just fit in one more on -- you had mentioned some additional formulations or SKUs or something in 3-IN-ONE product. Can you distinguish for us how that's positioned in the market versus WD-40 as a product? And then if you can give us some idea as to what these additional things might be?

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

Yes. Sure. Some of them are out there now. The 3-IN-ONE is basically precise delivery one drip at a time. And we've already launched a couple of extensions of the 3-IN-ONE system with what we call our Marksman delivery system, which is an extendable tube on our 3-IN-ONE brand. But it's basically taking solutions to the end-user under the 3-IN-ONE brand in the lubricant and protection category with a different delivery system than WD-40.

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

Okay. And then -- so that would mean it wouldn't be really cannibalizing of WD-40. It would be something new and incremental to the whole --?

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

No, no, no. No, no, no, no. The end-user has a different need and the delivery system does. And they may be a little cross but it will not cannibalize WD-40 any way at all.

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

Okay, great. And then just one last one. On your nonstrategic cleaning -- homecare and cleaning businesses, what specifically are you, like, doing? I mean, are you -- what would make you decide to auction off the business -- hold an auction and actually sell the businesses? And is the profit margin actually going up because you're cutting unprofitable SKUs and A&P spending, so the margins are actually going up?

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

Well, I'll answer that second one first. Yes, that's exactly what's happening. We have reduced a number of SKUs and a number of kind of promotional activities that were just not generating the level of profitability that we'd like. As -- reflected in that, we've seen a pullback in sales. As far as our decision to auction it, we are comfortable with holding it. We see the cash flow from it as being -- well, as embedded in some of our expectations. So it really would take somebody coming along saying, hey, these are a fit for us. And we want to be able to take these and leverage them in some way that's beyond what we see for them. We see our ability to continue to operate and execute in a harvest mode. If somebody wanted to pay us a premium to change them, we'd be more than interested in entertaining the offer.

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

And remember too, we're really primarily speaking about them in the United States. The 1001 business in the UK and our business down in Australia are a little bit different. So, if we were to exit any of them, it would only be in the US at this time.

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

Okay, very good. Thank you for your help.

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

Thanks, Linda.

**Operator**

And that does conclude today's question-and-answer session. Mr. Ridge, at this time, I'd like to turn the conference back to you for any additional or closing remarks.

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

Thank you for joining us today. Just a reminder that our next earnings conference call is scheduled for Tuesday, April 8, 2014, at 2 p.m. San Diego time. And until we talk to you again, we hope you stop some squeaks. Have a good afternoon.

**Operator**

And again, this does conclude today's WD-40 Company first-quarter 2014 earnings release conference call. We thank you again for your participation.

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