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Cornerstone Building Brands, Inc. (CNR)

Q1 2020 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by, and welcome to the Cornerstone Building Brands' First Quarter 2020 Earnings Conference Call. At this time, all participants are in a listen-only mode. After the speakers' presentation, there will be a question-and-answer session. [Operator Instructions]

I would now like to hand the conference over to your speaker today, Tina Beskid, Vice President of Finance and Investor Relations. Thank you. Please go ahead.

Tina Beskid

Vice President - Finance and Investor Relations, Cornerstone Building Brands, Inc.

Good morning, and thank you for your interest in Cornerstone Building Brands. Joining me today are Jim Metcalf, Chairman and Chief Executive Officer; and Jeff Lee, Executive Vice President and Chief Financial Officer.

Please be reminded that comments regarding the company's results and projections may include forward-looking statements that are subject to risks and uncertainties. These risks are described in detail in the company's SEC filings, earnings release and our investor presentation. The company's actual results may differ materially from the anticipated performance or results expressed or implied by these forward-looking statements.

In addition, management will refer to certain non-GAAP financial measures. You will find a reconciliation of these non-GAAP financial measures and other related information in the earnings release and investor presentation located in the Investors section of our website. Please note we will be referencing our investor presentation throughout today's call. Today's call is copyrighted by Cornerstone Building Brands. We prohibit any use, recording or transmission of any portion of the call without our expressed advanced written consent.

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Throughout this presentation, management may also refer to pro forma financial results. Such pro forma results give effect to completed acquisition, as if such acquisitions were consummated prior to the periods presented. Questions will be taken at the end of the prepared remarks.

With that, I would like to turn the call over to Jim.

James S. Metcalf

Chairman, Chief Executive Officer & Director, Cornerstone Building Brands, Inc.

Thank you, Tina, and good morning. We appreciate all of you joining us this morning. We really hope you and your families are safe and healthy during these turbulent times. Today, I'd like to begin the discussion on the actions that Cornerstone Building Brands are taking to address this extraordinary situation. While uncertainty exists, we are focused and aligned to lead our company through this pandemic stronger and we remain steadfast in our long-term fundamentals of our business.

We've been focused on three key areas; the health and safety of our employees and our communities; servicing our customers; and maintaining a strong financial position with a keen eye on liquidity as well as cash flow and capital discipline. The health and safety of our employees and communities is our number one priority. The US Department of Homeland Security has designated our industry as life-sustaining and essential.

Our products are necessary for new home construction, critical home repairs, and vital projects like hospitals and medical centers. We've taken extraordinary measures and invested in practices that help keep our employees safe at work. These actions include, additional cleaning of our facility, staggering crews, incorporating visual cues to reinforce social distancing, and providing face coverings and gloves, as well as implementing daily health validation.

Many of our policies and practices have been deemed best in class by local assessors and have been used by other companies. I'm also very proud of the innovation that our employees have shown as they support one another and the communities where they live. For example, our Middletown, Ohio plant is producing hand sanitizer to distribute to other plants that need this important product. And at our innovation center, our teams design cloth face masks that are being shipped to other manufacturing sites.

And finally, we've partnered with the National Association of Manufacturers donating safety supplies to those who are on the frontline of this health crisis and as we work to keep our communities safe, I'm proud to say we're the cornerstone of many communities.

Our second area of focus is servicing our customers. Across the business, our teams are in constant virtual communication with customers along with suppliers and government officials to maintain business continuity without disruption. We are currently operating all of our manufacturing facilities, distribution centers and installation services. We have been flexible effectively managing production schedules in response to short-term shutdowns for extensive cleaning, big shut downs and other changes in demand due to this pandemic. We know that it's more important than ever to meet our customer needs and strengthen our relationships.

Within our Commercial business, we received orders for COVID-19 stand-up medical and test facilities here in the US and in Canada. And I'd like to acknowledge and thank our employees for working in our manufacturing plants and throughout our organization with this unwavering dedication and commitment to serving our customers. We safely cover the market with value-added services and solutions to our customers and we thank our customers as well.

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We also remain diligent on preserving our solid financial position, which is our third area of focus. We've taken decisive actions to manage discretionary expenses and implement meaningful initiatives that will adjust the company's cost structure and such as recent consolidation of plants in Ambridge, Pennsylvania and Cambridge, Ohio and continued delayering of our commercial business to get our associates closer to the customer. The care of our company's employees, our customers, and our cash are the foundation that we're operating on.

Now, turning to slide 4. We started 2020 very strong delivering pro forma adjusted EBITDA of $98 million in the first quarter, which exceeded the top end of our guidance range and delivered the third consecutive quarter of year on year margin expansion in all segments. We delivered 210 basis points of pro forma adjusted EBITDA margin expansion over the first quarter of 2019. This increase in part was driven by our ongoing commitment to automation investments and lean manufacturing, which lowered our cost base and drove operational excellence across our entire organization.

Late in the quarter, we responded with speed and intensity to combat the effects of this crisis and leveraged our resilient business model to manage through the near-term challenges and positioned us to capture maximum benefits during the recovery. As you can see by our first quarter results, we came into this crisis strong and with great momentum. Our team is now focused on navigating this current crisis to emerge even stronger.

Cornerstone Building Brands' unique business model positions us well to navigate through these uncertain times. Our extensive operating footprint provides us with the flexibility to manage production schedules to ensure that our customers continue to receive our quality product without disruption. Additionally, we've put a heavy emphasis on optimizing our supply chain network, rationalizing our plant footprint particularly in commercial, and a continued focus on working capital improvement.

Now, turning to slide 5. Our broad portfolio of products and vast manufacturing network enables us to participate in a diversified set of end markets, new residential, repair and remodel, commercial, and manufactured housing that provides us with a unique strategic advantage.

The near-term outlook for our end markets are challenged. Single-family housing starts have dropped since the beginning of the first quarter, but homebuilding has been deemed an essential service. And interest and mortgage rates have remained low in an effort to boost the housing market. These near-term effects have the greatest impact on our residential businesses as our products are available through our retail channels, our customers, and installed on homes 90 to 120 days after construction began.

The impact on the nonresidential end markets are mixed. We have a broad and diversified set of product offerings such as engineered building systems, components, insulated panels and wall systems that serve a diverse and extensive set of market subsection, each of which are being impacted differently by the crisis. So far, the retail and manufacturing market are expected to be meaningfully lower, while warehouse, a significant market we participate in, remains stable from the strength of e-commerce.

For the month of April, net sales were down about 25% compared to pro forma prior year. We believe the results we experienced during April is an indicator for the rest of the quarter and anticipate second quarter net sales to be in line with April or slightly better due to improved backlogs. We know that times like this requires strong leadership and swift decisive action to preserve our financial strength and ensure sound liquidity. Our leadership team has experience successfully managing through downturns and has executed with speed to improve cash generation, lower cost and accelerate operational improvements.

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Now let's turn to slide 6. We exited 2019 with a disciplined focus on delivering results for our shareholders and our customers, by permanently reducing the operating cost structure of the business by over $110 million. Faced with the effects of this pandemic, we intend to capitalize on the momentum that we created last year and are targeting between $80 million and $100 million of structural cost improvements this year. These actions are rooted in our strategy to make Cornerstone Building Brands a lean, more agile, customer-focused company and position us to deliver profitable growth as the market recovers.

We have also taken prudent and precautionary steps to maintain our financial flexibility and liquidity. We've increased our borrowing under the ABL facility and cash flow revolver, resulting in a unrestricted cash on hand of approximately $476 million at the end of the quarter. We believe we have ample liquidity and it will be further supported by significant cash generation actions of more than $100 million primarily from effective working capital management and reduced capital spending.

While reducing costs and generating additional cash are important areas of focus for us, we have not lost sight of the need to continue to invest in our business for the long term. We remain committed to innovation and investing in new product introductions that will continue to grow our value proposition to our customers.

Certainly there are a number of variables that are unknown at this point including the full duration, the magnitude, the pace of the recovery across our end-markets. We've evaluated a number of possible scenarios and are confident that our actions we're taking combined with the company's existing financial position and sound liquidity will enable us to navigate whatever challenges come our way, so we can get to the other side stronger.

Now, I'd like to turn the call over to Jeff, who's going to walk through some of our financial results. Jeff?

Jeffrey S. Lee

Chief Financial Officer & Executive Vice President, Cornerstone Building Brands, Inc.

Thanks, Jim, and good morning, everyone. I would also like to express my gratitude to our employees for their commitment to a healthy and safe working environment as they continue to engage with our customers, suppliers, and other partners. In light of COVID-19, our financial actions remain focused on cost reduction, cash preservation, and ensuring near-term financial stability, which will serve us well as we manage through this uncertainty and benefit the company as the markets begin to recover.

Starting on slide 8, pro forma net sales for the first quarter were $1.1 billion, up 3.1% from pro forma net sales for the first quarter of 2019. Improved market sentiment across all segments coupled with additional shift days drove higher volumes during the quarter. Price and mix were favorable as compared with pro forma first quarter of 2019 as we continued our price discipline and further positioned Cornerstone Building Brands as both a market and industry leader in exterior building products.

Pro forma first quarter adjusted EBITDA was approximately $98 million or 8.7% of net sales, which exceeded the top end of our guidance range. We delivered 210 basis points of margin improvement, the third consecutive quarter of year-over-year expansion in all segments.

Favorable price and mix in the Windows segment and Siding segments coupled with favorable spread per ton in the Commercial segments generated $37 million of price and mix, net of inflation. As discussed during our call in February, we are now reporting savings net of cost as we remain focused on continuous improvement and lowering our overall cost structure. Offsetting these gains were high direct labor cost due to our readiness efforts to serve the previously anticipated second quarter seasonal demand increase.

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Additionally, compensation and other benefit costs were higher compared to first quarter of last year because of the employee related headwinds, as we anticipated and discussed during our last earnings call. Given the changes in demand due to the COVID-19 pandemic, we have taken actions to mitigate these impacts and to right-size the cost structure.

Now, let's look at our business segment results. Our teams focus on executing our strategy of operational excellence and profitable growth has resulted in margin expansion in all segments for the third consecutive quarter. As we manage through the uncertainties caused by the COVID-19 pandemic, our actions are rooted in strategy and margin enhancement is one of our guiding principles.

Turning to slide 9, in the first quarter, Windows net sales were $448 million, up 6.4% from first quarter 2019. The increase was primarily driven by healthy end markets and favorable selling price and mix across the US and Canada. Windows gross profit margin for the first quarter of 2020 was 16.5%, up 170 basis points on a pro forma basis as a result of price discipline, favorable product mix net of inflation, and realized cost savings.

Turning to slide 10, Siding segment pro forma net sales for the first quarter was approximately $249 million, 3% higher than the same pro forma period last year. The increase was driven by volume, price and mix. Pro forma gross profit margin was 24.6%, up 230 basis points compared to the pro forma prior year quarter primarily as a result of lower material cost, favorable price and mix.

Moving on to the Commercial segment on slide 11. Net sales for the quarter of 2020 were $424 million, about flat with the same period last year. Overall, average selling price per ton was higher as a result of better product mix and price discipline, which was offset by lower tonnage volumes. For the quarter, gross profit margin was 23.1%, up 180 basis points year-over-year, driven by favorable spread, partially offset by higher variable manufacturing costs.

Turning to slide 12. Although it's still too early to determine the extent and duration of the COVID-19 impact on our business and the overall economy, we can report that net sales for April were down 25% pro forma last year. All segments were impacted with declines of 22% to 28% in US residential, approximately 43% (sic) [20%] (18:08) in Canada, and 20% in our commercial business. As such, we anticipate second quarter net sales to be in line with or better than April's results compared to the pro forma period last year. As such, based on April results and our current views of the market, we anticipate second quarter net sales to be in line with or better than the pro forma second quarter 2019.

In response to these unprecedented times, we have implemented aggressive near-term expense control actions that we believe will help offset the impacts from lower volume. We've also accelerated strategic structural expense reductions that will position Cornerstone Building Brands to be a leaner, more agile, and more customer-focused organization.

We took decisive action to align our cost structure with the decline in volumes. The decremental margin impact from lower volumes is approximately 30% on a consolidated basis. With some segments higher and some segments lower, our direct cost structure is mostly variable as approximately 10% of our cost of goods sold is comprised of fixed cost such as lease, utility, taxes, and other fixed expenses.

We reduced production schedules to align with customer demand while continuing to serve our customers without disruption. Additionally, we have implemented demand-related employee furloughs. We will continue to monitor our order rates and adjust furlough plans going forward as necessary.

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Across the company, our teams are working diligently to reduce near term-related discretionary spending. This includes eliminating travel, implementing hiring freezes, and delaying wage adjustments, merit pay increases, and other variable compensation programs. These actions will provide between $40 million and $60 million of savings in 2020 and will improve the decremental margins mentioned earlier. Since the business environment under COVID-19 is still fluid and evolving, it is impossible to predict what the ongoing impact will be. So we will remain flexible and adjust our near-term responses as necessary in order to preserve our solid financial position.

We plan to remain committed to our strategic priorities of improving our customer experience, operational execution, and strong financial performance. We have demonstrated our ability to reduce structural costs in many areas of the business including material sourcing, plant and back office rationalizations, process and labor savings from automation, and many others. Previously, we communicated that we would deliver $60 million of structural cost savings in 2020. As we face this pandemic, we remain committed to delivering these continuous improvements in structural savings along with accelerating other initiatives to simplify our manufacturing footprint and organization.

For example, within one of our Commercial plants, we are improving the semiautomatic frame production line by installing state-of-the-art robotic welders during the final stage of assembly, permanently reducing man-hours per ton, consuming less welding supplies, and preventing costly rework. In total, we now expect to reduce structural cost by $80 million to $100 million in 2020.

The resiliency and sustainability of Cornerstone Building Brands' business model is built upon a strong execution culture. Our market leadership positions across highly diversified channels and a broad portfolio of products, which is led by a team with proven experience in successfully navigating similar challenges. As a result, we expect to emerge as a stronger company.

Turning to slide 13, I would like to make some comments about our balance sheet and liquidity. Our free cash flow usage of $30 million in the first quarter was better than prior year as a result of delivering higher pro forma adjusted EBITDA, lower cash taxes, and effectively managing working capital. First quarter is typically a low point for free cash flow due to the seasonal nature of construction activity.

We expect a significant step up over the rest of 2020, as it will reflect favorable working capital performance and the impact of our initiatives to reduce structural cost and other near-term expenses. In addition to cost savings, we have also put similar controls on cash and liquidity management, including the reduction of capital expenditures by approximately $30 million.

While managing cost and generating additional cash are important areas of focus, we have not lost sight of the need to continue to invest in our business for the long-term. We remain committed to innovation and investing in new product offerings and process automation that will generate profitable growth in the future. We have been actively managing working capital, optimizing our purchasing actions and working with our key supplier partners. We anticipate that effective working capital management will be a source of cash in 2020 between $100 million and $120 million.

In the area of taxes, we are taking advantage of COVID-related government stimulus programs to defer certain payroll and income taxes to later in 2020 or in some cases into 2021. Additionally, provisions with the CARES Act will allow the company to deduct higher interest expense for income tax purposes that would have been previously disallowed.

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We expect these actions to have a net cash tax benefit of approximately $25 million in 2020. We ended the quarter with approximately $476 million of unrestricted cash on hand and $118 million of excess availability on our asset-based revolving credit facility. Our liquidity is sufficient to weather the anticipated slowdown in construction activity from the impact of the COVID-19 pandemic. We have no significant debt maturities until April 2023, which is when the cash flow revolver and asset-based revolving facilities mature.

In addition to the lack of near-term debt maturities, a key aspect of our flexible debt structure is the absence of any restrictive standing maintenance financial covenants. The cash flow revolver does have a financial covenant set to a maximum secured leverage ratio of 7.75 to 1, however, we have sufficient cushion that prevents this covenant from being a concern. Our liquidity testing has included many challenging scenarios, and under such scenarios, we expect to have ample liquidity to navigate this period of uncertainty.

Turning to slide 14. Over the past few months, we have taken quick and decisive actions to reduce operating expenses and defer capital expenditures with the objective of maximizing our available liquidity. We plan to stay disciplined on price, drive profitable growth and capture additional savings.

Additionally, we plan to generate significant cash from focused working capital management, while we remain committed to our capital allocation priorities. We are proud of the continuous improvement culture we have created as demonstrated by our three consecutive quarters of margin expansion in all segments.

And now, I'd like to turn the call back over to Jim for some closing remarks.

James S. Metcalf

Chairman, Chief Executive Officer & Director, Cornerstone Building Brands, Inc.

Thank you, Jeff. We at Cornerstone Building Brands are committed to our customers and to creating great building solutions. We've always known that Windows matter and it's a vital product category in our portfolio.

Now, during the COVID-19 crisis you may have noticed that Windows have quickly become even more important to our communities. We are proud to offer products that are helping people stay safe and connected to loved ones as we face this pandemic.

As I mentioned at the beginning of the call, the safety of our employees is our number one operating principle and transparent communication is a top priority. We are committed to keeping our employees safe.

Today we discussed the actions we've taken so far, our current plans and our thoughts for our business as we move forward. However, the current dynamics are fluid and still evolving. It's impossible to predict what the ongoing impact will be. So, we're going to remain flexible and adjust our responses as necessary.

In terms of our financial priorities, we remain focused on improving our cash generation and managing the decremental margins. Our disciplined culture is committed to delivering margin improvement from a focus on operational excellence every day. I believe the proactive measures we are taking and the strength and the long-term fundamentals of our business will enable us to emerge from this downturn even stronger.

Thank you for joining us this morning and please stay safe. And now, we'll open up the call for your questions.

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QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Our first question comes from the line of Lee Jagoda of CJS Securities. Please go ahead. Your line is open.

Lee Jagoda
Analyst, CJS Securities, Inc.

Q

Hi. Good morning.

James S. Metcalf
Chairman, Chief Executive Officer & Director, Cornerstone Building Brands, Inc.

A

Good morning, Lee.

Jeffrey S. Lee
Chief Financial Officer & Executive Vice President, Cornerstone Building Brands, Inc.

A

Good morning, Lee.

Lee Jagoda
Analyst, CJS Securities, Inc.

Q

So, can we start with the structural cost reductions and then the near-term cost managements. It sounds like on the cost reduction side, it's an incremental 20% to 40% versus what we're originally kind of contemplating here. And then on the other piece, that's more of a new item. Is there a way on each of those to break up the expected savings between cost of goods sold and SG&A?

James S. Metcalf
Chairman, Chief Executive Officer & Director, Cornerstone Building Brands, Inc.

A

Yeah. Lee, this is Jim. Just to kind of put it in context, if you recall when we put the companies together to form Cornerstone, we had a three-year plan. From 2018, we had $25 million of cost reductions. Last year, we identified and hit $110 million. And then, as we said in our comments that for 2020, we have identified an additional $60 million, which obviously includes some of the things that Jeff talked about SG&A, furloughs, delayering the organization. So, I just wanted to put that in context of we don't want to lose sight of the fact of the cost reductions that we've committed to our shareholders with the combination of Cornerstone.

So, with that, I'll turn it over to Jeff and he will give some additional color on our – as you say, some of the new cost reduction initiatives that we've put in place because of COVID-19.

Jeffrey S. Lee
Chief Financial Officer & Executive Vice President, Cornerstone Building Brands, Inc.

A

Great. Thanks, Jim. So, Lee, as we think about are our cost-out initiatives, it's important to recognize that we have speedily and with a lot of actions with the management team to make sure that we're taking out the costs appropriately and managing through this crisis. We're starting at the top and just making sure people understand how we're thinking about the business, from a volume perspective. Before we look at the cost initiatives, we're expecting the impact on margins to be about 30%. So as volume comes down, the volume would come down with the 30% rate.

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Now to offset some of those things, we're taking some dramatic actions within the company to make sure that we have preserved liquidity and also that we're restructuring the company so we can come out of this crisis in a stronger, bolder, and better position. So as you mentioned, we have taken out short-term or near-term $40 million to $60 million of anticipated cost actions that will result in 2020.

Now, these are – some of these are volume-related. So as volume comes back, we would expect some of those costs to come back with that such as some of the compensation when it comes to sales engineers and the like. Travel expenditures is probably another good example as you think about the lift that's coming off of traveling, going back out, meeting with our customers. Those types of things will start to ease as we start to feel better about the situation.

But more importantly, as we think about the structural cost reductions, the $80 million to $100 million of which we referenced, $60 million of that was identified and communicated as we came into 2020 and so, those are permanent type of reductions versus the temporary ones that I've mentioned above. And they include things like the back office rationalization, manufacturing footprint, consolidation of some of those facilities, and many continuous improvement types of cost out initiatives.

So, we're proud of what we've been able to do as a management team managing through this crisis. Specifically, talk to answer your question as we think about cost of goods sold and SG&A. For both categories, the near-term and also the structural cost, they're about 60% related to cost of goods sold and 40% coming out of SG&A.

Lee Jagoda
Analyst, CJS Securities, Inc.

Q

Got it. And just switching to the segments maybe if I can. Within each segment – and I appreciate the 30% decremental EBITDA margin commentary in total. Within each segment, is there a way to either rank order or give us some more clarity by segment in terms of the – what the decrementals might look like?

Jeffrey S. Lee
Chief Financial Officer & Executive Vice President, Cornerstone Building Brands, Inc.

A

I think that as you look at historical segment data we provide, we do have gross margins by segment, and that's a great way to think about the difference potential between the different segments that we have. Keep in mind, there's about 10% fixed expense within our gross profits. And so, then, you can kind of back from there into the variable margin or contribution margins that we would expect by segment.

Lee Jagoda
Analyst, CJS Securities, Inc.

Q

Got it. And I just want to make sure I got your guidance right. So, if I take your pro forma Q2 revenue that's in the back of your slide deck, you're basically saying that April was down 25% versus the April of last year. And then for the quarter, we should expect it to be 25% down or better than that for the remainder of the quarter. Is that – am I thinking about that correct?

Jeffrey S. Lee
Chief Financial Officer & Executive Vice President, Cornerstone Building Brands, Inc.

A

Yes. That is accurate.

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Lee Jagoda
Analyst, CJS Securities, Inc.

Q

Okay. And then just a follow-up to that, is there anything you can comment on with regard to the last – the first two weeks of May versus April? And whether that trend has flattened or potentially gotten a little better as states start reopening.

James S. Metcalf
Chairman, Chief Executive Officer & Director, Cornerstone Building Brands, Inc.

A

Lee, this is Jim. That's a great question. We have seen some positive green shoots, nothing to ring the bell on, but we started to see our bookings have improved. We're starting to see also in the retail segment with some of the stores having extended hours. The point of sale has improved particularly in the last two weeks. And quite frankly with some of the states opening up in the Midwest, Michigan, Pennsylvania, Ohio, where job sites now are starting to get lifted. We – our customers are starting to replenish inventories. So, we don't want this to be a false positive, but it has improved in the last couple weeks.

Lee Jagoda
Analyst, CJS Securities, Inc.

Q

That's great. I'll hop back in queue. Thank you very much.

Operator: Our next question comes from the line of Andrew Casella of Deutsche Bank. Please go ahead. Your line is open.

Andrew Casella
Analyst, Deutsche Bank Securities, Inc.

Q

Hi, Jim, Jeff. Thanks for taking the questions and glad to hear you guys are doing well. To follow-up on some of the color on the second quarter, have you gotten the sense that some of what you're seeing as an uptick in the last couple of weeks, if that's jobs that were previously booked, just finally getting around and getting those started? Or do you feel like demand is actually improving?

I guess, what I'm trying to vet out there is, I guess, implied in your commentary is that May and June will improve off of April just given that the ceiling is 25% and should be better than that for the second quarter. But curious if you have any additional color on that.

James S. Metcalf
Chairman, Chief Executive Officer & Director, Cornerstone Building Brands, Inc.

A

Yeah, I really think it depends on geographic – where you are geographically in product segments. As I just mentioned, the states that are lifting in the Midwest is really positive for residential business, particularly our Siding business that's strong in that part of the world, where inventories are getting replenished, but also people are finishing up jobs.

On the Commercial side, there's still some limitations on how many people can be on jobs. And that is a state by state. But we are in this – the traditional season as well. So jobs are trying to get finished up, both residential and commercial. Some inventories are getting replaced from our dealer standpoint. And then in our large retailers, as I said, are expanding store hours from where they were a month ago and are also replenishing some inventory.

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So again, it's – there are some positive signs over the last couple weeks, but we are taking a conservative approach. We want to focus on the cost reductions that Jeff and I have alluded to. We have contingency plans if things don't improve. But this is a week by week initiative. We have a – this is a local ground game as well. As you know counties can change. The Bay Area changes in California almost on a weekly basis, which impacts our installed stone business. But there are some areas for example in the Minnesota area, where business is quite strong for other environmental stone business.

So, it is very geographic. It's very product specific. And we have a – we've put in an enriched sales and operation planning process that we really look at, not only housing starts and AIA, and all the traditional metrics. But we're starting to look at what's happening from accounting standpoint and really what's happening with what states are coming back and our impact there. So, last couple weeks there are some positive signs, but I don't want to say that that is going to be permanent.

Andrew Casella
Analyst, Deutsche Bank Securities, Inc.

Q

Okay. That's helpful color. And then clearly with you guys being a [ph] huge (38:02) buyer of resin, can you help us understand a little bit about the pricing environment, your kind of net cost as we think about lower resin, the impact [indiscernible] (38:11) how you guys are kind of thinking about that flowing through in the numbers.

James S. Metcalf
Chairman, Chief Executive Officer & Director, Cornerstone Building Brands, Inc.

A

Yeah. It's a great question. So, we did well with price increases inside of our residential business typically inside of the first quarter and that can bleed into the second quarter as well. And those announcements have gone out and we have begun to realize price similar to 2019.

And so we feel good about our pricing actions that we've put in place and we feel good about our service proposition and the value that we have for our customers and they recognize the benefit that we have with our global manufacturing and our national manufacturing footprint and our ability to serve our customers across multiple regions, especially during these type of environments. I think, they appreciate the fact that we can manage through these type of crisis in specific regions, where we have to slowdown production or stop production, we can shift that into different areas. And so it gives us a real advantage for our customers to not only ask for the price, but get the price.

From a commodity perspective, it kind of goes up and down, and it depends on which business you're looking at and also the labor market. Depending on where you're looking at, you can see pressures coming in from that. So, we are – right now, we're assuming stable pricing across or stable cost across our commodities. And that does change on a very frequent basis, and so we're monitoring that appropriately.

Andrew Casella
Analyst, Deutsche Bank Securities, Inc.

Q

Okay. Great. And then a final question from me just on liquidity and cash flow. So, just to confirm, the $118 million of excess availability, is that actually available or are there any [ph] springing (39:55) covenants that we should be mindful of? And then also to the extent you guys seem like you'll be generating a bunch of cash flow, just priorities as you think about it, the – I know you guys have done small bolt-ons in the past. Obviously, stuff is coming to become more attractive from a valuation perspective. Your debt is trading below face value. Just kind of curious how you guys think about it internally and capital allocation?

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Jeffrey S. Lee
Chief Financial Officer & Executive Vice President, Cornerstone Building Brands, Inc.
A

Yeah. So, to your first question about the liquidity itself, so we do have availability remaining on our asset base loan revolving facility, and there's no restrictions on that. And so, it is available to us today. It does modify and change based on the level of receivables and inventories that we have. So, there's no restrictions on that amount and we feel comfortable that with the liquidity we have in hand that we're going to be able to continue to manage through this without any issues.

Specifically around the capital allocation, the way we're thinking about it, first of all, we'll continue to run the business and make sure that we've got the right investments going in around our maintenance capital, and keeping our plants running and making sure we're as efficient as we can be. But we're going to continue to invest inside the company, from a growth perspective, to make sure we've got new products that are coming out and innovation.

We're going to further continue to invest inside of capital projects that make sense for the company and have good returns for our shareholders. So, those projects are first on our list as we think about capital allocation. And then we'll think about things as acquisitions and debt paydown as other priorities for us, acquisitions obviously looking at those that will meet our acquisition criteria which is very strict. And then debt paydown is appropriate and we still have our guidance that we'd like to maintain, which is to get us to that 2% to 2.5% – or 2 times to 2.5 times over the long run.

Andrew Casella
Analyst, Deutsche Bank Securities, Inc.
Q

Okay. Great. Thanks so much, guys, and stay safe.

Operator: Our next question comes from the line of Matthew Bouley of Barclays. Please go ahead. Your line is open.

Matthew Bouley
Analyst, Barclays Capital, Inc.
Q

Hey. Good morning. Hope everyone's doing well. Thanks for taking the questions.

James S. Metcalf
Chairman, Chief Executive Officer & Director, Cornerstone Building Brands, Inc.
A

Good morning.

Matthew Bouley
Analyst, Barclays Capital, Inc.
Q

I wanted to ask about the non-res backlog. I know you gave some helpful color on the verticals. I guess if you could elaborate a little if the backlog is giving you any sort of go forward visibility, and I guess what are you seeing or hearing in terms of cancellations versus projects being simply [ph] pushouts (42:32), how's all that shaping up? Thanks.

James S. Metcalf
Chairman, Chief Executive Officer & Director, Cornerstone Building Brands, Inc.
A

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Yeah. Thank you. That's a great question. What we saw in early April, we saw quite a bit of not cancellations but pushouts. We typically see pushouts in around the 10% range and they – the pushouts got upwards to 30%, 40%. That's come back down to our traditional ZIP code, but it really depends on the sub-segment. If you look at e-commerce warehousing, that business and – that business is still very steady. But if you look at typically anything retail, office, commercial, those jobs are – we'll finish but there's nothing on the books.

So, it really depends on where you are. Retail office is going to be challenged this year. Warehouses is also – that's going to be a positive in healthcare. So, it really depends on where we play. We're seeing bookings have improved really in the last couple of weeks. And the customers are really positive on the Commercial side. They want to get their jobs finished. They're concerned with – if you're in the retail Commercial side of the business, you're seeing things being stopped or pushed out. But if you're focused on data warehouses, e-warehouses, things like some – jobs like that, there's quite a few jobs that are on the docket that we're chasing right now.

So, we're being cautious about the Commercial next couple of months. As we said in our comments, we are rationalizing our plant footprint. We're looking at what is the best footprint to have from a demand standpoint going forward to service our customers. And also, we're delayering the organization to get really front and center with our customers with the decision makers. So, it's a mixed bag as some segments are going to be challenged. The retail segment, the office segment as I said, industrial manufacturing will be challenged. But healthcare, e-warehouse, we think there's some opportunities there.

Matthew Bouley
Analyst, Barclays Capital, Inc.

Q

Got it. That is very helpful, Jim. So the – I mean the follow-up to that, I guess, would be, I mean, since there does seem to be such large variations in the verticals, are there any sort of margin differentials for Cornerstone related to different product mix on those that we should be aware of going forward? And the assumption is that, some of these trends might be persisting for an extended period. Thank you.

James S. Metcalf
Chairman, Chief Executive Officer & Director, Cornerstone Building Brands, Inc.

A

Yes. Thank you. And there are – definitely we look at each segment, what the margin is in each segment, and we really balance as Jeff said, we balance price and volume with looking at margins. Quite frankly, there are some jobs that we will pass on because the margin profile isn't something that we want to participate in. We would rather have competition take a job like that. So we're very focused on the segments, the margins, not only on the Commercial side but we look at the same pricing strategy on the residential side by customer, by repair and remodel, also by end-use market.

So that is a really core competency that I'm extremely proud of what our organization has done over the last couple of years of really looking at the value proposition of Cornerstone, getting the value, where the price and volume mix, how you balance that. And really, it's extremely important particularly on the Commercial side where you see steel prices have been moving down. And we want to make sure that we balance price and volume with our cost structure.

So we have processes in place. We have internal software that tracks our pricing. We have pricing policy individuals that really monitor our pricing strategy here. And I'm really proud of the results that we've had over the last couple of years on pricing. And we'll continue to be strategic on balancing price volume and margin as we go forward.

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Matthew Bouley
Analyst, Barclays Capital, Inc.

Q

Got it. Very helpful. Hope everyone stays well. Thank you.

James S. Metcalf
Chairman, Chief Executive Officer & Director, Cornerstone Building Brands, Inc.

A

Thank you.

Jeffrey S. Lee
Chief Financial Officer & Executive Vice President, Cornerstone Building Brands, Inc.

A

Thanks, Matt.

Operator: Our next question comes from the line of Zane Karimi of D.A. Davidson. Please go ahead. Your line is open.

Zane Karimi
Analyst, D.A. Davidson & Co.

Q

Hey. Good morning. Two quick questions for you guys. Are we still planning to bring down debt by that three quarters to a full turn by year-end? And then also with the CapEx spend what percent can we be attributing to growth focused initiatives versus like more maintenance?

Jeffrey S. Lee
Chief Financial Officer & Executive Vice President, Cornerstone Building Brands, Inc.

A

Yeah. So, Zane, let me talk about both of those. There's still a lot of uncertainty right now around the forecast for 2020. And so, it's very difficult for us to talk about where the leverage ratio might be at the end of the year. And so, we pulled our guidance on kind of full year and because of that we also want to make sure that we're not giving guidance right now on the leverage ratio that could be anticipated.

We are looking at a lot of different scenarios that are out there, but at this time we want to continue to make sure we understand the demand forecast and our volume assumptions before we committed to that. Long-term – just to reiterate, long-term we're still committed to getting our leverage ratio down to that – to those low-2s that we talked about. And so that's the commitment we have.

The second question on CapEx, it's a good question and we're focused as an organization making sure that we put the priority on the projects, and the things that will create the most value for the company. We have about $30 million to $40 million worth of maintenance CapEx as a company. And that's just to kind of keep things running, keep our equipment up and fresh and making sure it's efficient and keeping it safe for our employees.

And so, that will continue, right, and we'll make sure that we're investing those dollars appropriately for the business. And then the rest of the CapEx we really prioritize, right? It's a real process we go through as an organization to make sure that we're putting those projects that have growth in front of them first and making sure that we are investing appropriately, so that we can continue to maintain organic growth rates within the company.

And then second, we look at those projects that have the highest return on investment or for the safety of our employees, right? And so, we balance those to make sure that we're appropriately managing that spend that we have.

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Zane Karimi
Analyst, D.A. Davidson & Co.

Q

Thank you. And then can you talk about any pockets in the US or even Canada that have experienced greater COVID impacts with regards to like customer demand?

James S. Metcalf
Chairman, Chief Executive Officer & Director, Cornerstone Building Brands, Inc.

A

Yeah. Obviously, the first outbreak was in the State of Washington, and they – the state seemed to get on that pretty extensively. Really, the northeast is obvious. Everyone watches the news. It's the New York, New Jersey area. Also, we've seen some hot spots in Atlanta and Dallas where there have been some outbreaks as well. But really the key area and I believe most – half of the cases are in that New Jersey, New York area.

And I will say that I am extremely, extremely proud of the job that our entire team has done on the safety of our employees. We've been told by outside experts it's industry leading, we've been very aggressive about deep-cleaning our facilities, doing temperature checks of all of our employees, mask, when there's any doubt of its safety or volume, we lean on the safety side. Safety is a core value of Cornerstone and it's something that we swung into action, as Jeff said in his comments, very decisively, proactively.

We have a crisis management team that is led by the senior management team of the company. We meet sometimes not only on a daily basis but on hourly basis, particularly in April when things were changing so fast you saw a lot just – it was a state-by-state, county-by-country [ph] grounding (51:27) that we jumped into this. And I think everyone on this call, and I'm so proud of our employees at our plants that have gone there every day. They're our frontline heroes. But also what we've done as to having the safety of our employees and our customers to get through this terrible crisis.

We feel we're maybe in a little bit of a stabilization in the middle of this crisis. And we've gotten used to this thing but every day something changes. We are going – we have contingency plans, as Jeff said, depending on if demand if gets worse. But also we've talked a little bit, there's some green shoots where there are some sustainable volume increases.

And what's great about Cornerstone is our extensive national footprint, where we can, if we idle a plant for deep cleaning, we can put that production in other plants. And I'm proud to say that we've done a really super job, and our customers have said this, of servicing our customers with undisrupted service here over the last six weeks. And we continue to – we plan to continue to do that.

Operator: Our next question comes from the line of Richard Kus of Jefferies. Please go ahead, your line is open.

Richard E. Kus
Analyst, Jefferies LLC

Q

Hey guys. Most of my questions have been answered here. But just quickly on the decremental margins, that 30% that you're talking about. Does that already include the benefit from the near-term cost saves that you plan to get or would you end up running that through, and then you end up getting the near-term cost saves that offsets some of that impact?

Jeffrey S. Lee
Chief Financial Officer & Executive Vice President, Cornerstone Building Brands, Inc.

A

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Yeah, Richard, I appreciate the question on that and clarification. So, the 30% is pre-action, right? So, take the volume assumptions, whatever assumptions you may have and bring it down by 30% and then add back those different near-term and structural cost benefits to get to a revised decremental rate.

Richard E. Kus
Analyst, Jefferies LLC

Q

Got you. That makes sense.

Jeffrey S. Lee
Chief Financial Officer & Executive Vice President, Cornerstone Building Brands, Inc.

A

And, Richard, maybe just talk a little bit about history, and we've done a lot of work and a lot of analysis around this as well. Going back to 2019 was a good example of what we've been able to do, right? So from 2018, we finished our EBITDA margins at 10.6% and in 2019, we increased that 130 basis points to 11.9%. And it was really a couple of things that drove that, right? We talked about the price strategy that we had net of some of the inflation. But we also communicated that we had about $110 million or we did have the $110 million worth of cost out inside 2019. So, it's a nice comparison as you think about the additional cost out that we're taking now, and you go back and look at 2019. I think it can help a lot of people understand the value that comes from these cost out initiatives that we're embarking upon.

Richard E. Kus
Analyst, Jefferies LLC

Q

For sure. And then in terms of the 40% to 60%, how much of that impact do you think you can get through the numbers in Q2 alone?

Jeffrey S. Lee
Chief Financial Officer & Executive Vice President, Cornerstone Building Brands, Inc.

A

So, estimating about $10 million from the 40% to 60%. And we – as Jim said and we both commented on, we are pretty quick in making decisions around the end of March as we started to see things turn a little bit south. And so, we quickly put a lot of these things in place to make sure we were maximizing liquidity and preserving as much profit as we could.

Richard E. Kus
Analyst, Jefferies LLC

Q

Got it. Okay. That makes sense. And then, lastly for me, in terms of working capital savings, you expect pretty impressive number there, how do you see the breakout between receivables, payables, inventory? Where do you see the most opportunity?

Jeffrey S. Lee
Chief Financial Officer & Executive Vice President, Cornerstone Building Brands, Inc.

A

Yeah. So, we're going to continue with our strategic objectives around working capital management. We have put, as we talked about last, year $50 million on working capital improvements coming from inventories, payables, and receivables, our primary working capital. We're going to continue with that, right? So, it's one of the things that we haven't slowed down on. It's a focus for us as a management team and as a company to make sure that we've got the proper amount of inventory in particular to run the company and service our customers appropriately.

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We put in a lot of effort around ourselves operating planning process within the company which has enabled us to have better visibility into customer demand, anticipate what might be happening and then putting our inventory levels appropriately to make sure we hit the service levels that our customers require of us. So, we haven't taken any focus off of that.

In addition to those things, we will continue to see a little bit of the recent trends inside of first quarter with some of the lower steel costs that are coming in that has a benefit on working capital. And then some of the volatile volume assumptions that we've seen as a reason also have some contributions to working capital.

Richard E. Kus
Analyst, Jefferies LLC

Q

Okay. That's great. Thank you very much.

Operator: Thank you. And our last question comes from the line of Andrew Casella of Deutsche Bank. Please go ahead. Your line is open.

Andrew Casella
Analyst, Deutsche Bank Securities, Inc.

Q

Hi. Thanks for taking the follow-up. I apologize if I missed this, but did you guys indicate what type of impact you were seeing at the tail end of March? I mean obviously you guys had a really good first quarter, but just curious if you started to see headwinds showing up towards the end of the month or that was more of second quarter?

Jeffrey S. Lee
Chief Financial Officer & Executive Vice President, Cornerstone Building Brands, Inc.

A

Yeah. It really started right after St. Patrick's Day, it was mid-March. The month of March was down about 5%.

Andrew Casella
Analyst, Deutsche Bank Securities, Inc.

Q

Okay. Great. Thanks so much.

Operator: Thank you. Ladies and gentlemen, this is all the time that we have for Q&A. This concludes today's conference call. Thank you for participating. You may now disconnect.

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