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HSC - Q1 2014 Harsco Corporation Earnings Conference Call

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CORPORATE PARTICIPANTS

Dave Martin *Harsco Corp - Director of IR*

Dave Everitt *Harsco Corp - Interim CEO*

Nick Grasberger *Harsco Corp - President, COO & CFO*

CONFERENCE CALL PARTICIPANTS

Jeff Hammond *KeyBanc Capital Markets - Analyst*

Glenn Wortman *Sidoti & Company - Analyst*

Scott Graham *Jefferies & Company - Analyst*

PRESENTATION

Operator

Good morning. My name is Brianna and I will be your conference facilitator. At this time I would like to welcome everyone to the Harsco Corporation first-quarter release conference call. All lines have been placed on mute to avoid any background noise.

(Operator Instructions)

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I would like to introduce Dave Martin of Harsco Corporation. You may begin your call.

Dave Martin - *Harsco Corp - Director of IR*

Thank you and welcome to everyone joining us today. My name is Dave Martin. I'm the Director of Investor Relations for Harsco.

With me today are Dave Everitt, our interim Chief Executive Officer; as well as Nick Grasberger, our President, Chief Operating Officer and CFO. This morning we will discuss our results for the first quarter of 2014, provide our outlook for the year and discuss our Metals & Minerals Improvement Plan or Project Orion.

Before our presentation, however, let me take care of a few administrative items. First, our earnings news release was issued this morning before the market opened. A PDF file of the news release, as well as the slide presentation that supplements our remarks for this call have been posted to the Investor Relations section of our website. We encourage you to access these files.

Secondly, this call is being recorded and webcast. A replay will be available on our website later today.

Next, we will make statements today that are considered forward-looking within the meaning of the federal securities laws. These statements are based on our current knowledge and expectations and are subject to certain risks and uncertainties that may cause actual results to differ materially from these forward-looking statements. For a discussion of such risks and uncertainties see the risk-factors section in our most recent 10-K and 10-Q, as well as in certain of our other SEC filings. The Company undertakes no obligation to revise or update any forward-looking statement.



Lastly, on this call we will refer to adjusted financial results that are considered non-GAAP for SEC reporting purposes. A reconciliation to US GAAP results is included in our press release issued today, as well as in our slide presentation. With that being said, I'll now turn the call over to Dave Everitt.

Dave Everitt - Harsco Corp - Interim CEO

Thank you, Dave and welcome everybody. Today, as Dave said, we're going to talk about two key elements on this call, the first-quarter results and 2014 outlook. And then we're going to talk about the Metals & Minerals Improvement Plan which we'll refer to as Project Orion.

Relative to the first quarter, we're very pleased with the results. End market dynamics and internal execution by the team here at Harsco had beneficial impacts this quarter and results are a positive result of that. Our Rail and industrial businesses are performing at good levels and we're encouraged by a firming of steel and nickel prices for the metals business and by the execution of the Metals & Minerals team. We'll talk more about that in our Project Orion conversations.

The first quarter benefited from some favorable timing. Contract renewal costs for Metals & Minerals were somewhat better than we expected and in Rail, we had some parts sales that were advanced into the first quarter and that had a favorable impact on the first quarter.

Our outlook for the balance of the year has not changed, excluding the benefits of Project Orion and we'll talk about that in a minute. Over all, the team and I feel very confident about our ability to deliver and achieve the 2014 goals.

Also let me make a comment on leadership transitions at this point in time. As you know, we've gone through a leadership transition here in the last few months. Nick has been named Chief Operating Officer and will be assuming the Chief Executive Officer role this year. That change has been broadly accepted by the organization. The organization has great confidence in Nick and he and I are working well together. Were very happy, as well, with some additions to our executive team and we're in the midst of an active search for a new CFO to relieve Nick of those responsibilities.

Let me just talk for a minute about Project Orion. Nick and the team, at the December Investor Day, indicated we'd be discussing the specifics of the Metals & Minerals Improvement Plan on this call. We're excited to share with you a program that we believe will create and deliver significant shareholder value over the next few years.

The project will lean out our cost structure and deliver a better contract mix. We expect Metals & Minerals free cash flow per annum to increase two to three times by 2017, and the ROIC of the business to nearly double by that same time.

This project is the culmination of many months of work by the Metals & Minerals team to define what we're doing, where we can add value and where we can improve it. Nick and the Metals & Minerals team have spent a significant amount of time going through a lot of detail and developed a plan that we're now in the execution phase of.

I'm also pleased with the addition of Rick Lundgren, our President of the Metals & Minerals business. He's joined us in the last month or so. He's quickly integrated into the business, developed the confidence of the team, and the leadership he's shown in that short period of time has been significant and I think he's a great add to the team.

I would also tell you that the Board has been very engaged in the development of this plan. At the last Board meeting we reviewed the plan in some detail and the Board has a high degree of confidence in the successful execution of the program.

Unlike previous efforts to boost the performance of the Metals & Minerals business, this effort, Project Orion, is a program that is broad and deep and is supported by a greater understanding of data inherent in the business. A more extensive analysis of that data, to make sure we understand the drivers of the various aspects of the business. And a stronger integration of external benchmarking information and I feel very good about the results.



At this time, I'd like to turn it over to Nick to talk about the quarterly results forecast for the year and a lot of detail about the Metals & Minerals business.

Nick Grasberger - *Harsco Corp - President, COO & CFO*

Thank you, Dave. Good morning, everyone. Thank you for joining us. I'll spend a few minutes talking about the Q1 results as well as the outlook for the balance of the year but spend most of the remaining time here talking about Project Orion.

So for those of you following on the slides, I'm on slide 3. As Dave mentioned, the first-quarter results were encouraging. We generated operating income of an adjusted basis of \$34 million versus our guidance of \$20 million to \$25 million. That's up about 5% versus the first quarter of last year. Each of the three business segments beat the expectations, and corporate costs were also a bit lower than we thought.

Dave acknowledged that timing accounted for a large portion of this variance. There were some contract renewal costs within M&M that we thought would be incurred in Q1, they will likely be incurred in Q2.

We also pulled forward some revenue in the Rail business around contract services and after-market parts. The corporate costs, as I mentioned, were also somewhat lower than we expected, but those will likely be incurred in the second quarter.

The markets in the first quarter actually began to firm in March. We had a weak start to the quarter. Many companies did due to weather related conditions.

But the month of March was quite strong. In particular, we saw nickel prices increase, steel production improve and natural gas prices firm as well. So March was a quite strong month across all of our businesses. In terms of Brand, the cash earnings in that business continue to be consistent with expectations. We'll talk more about Brand in a minute.

In terms of challenges for the quarter, free cash flow was, as you'll see, a bit better than expectations due largely to the deferral of capital spending in Metals & Minerals.

We also had difficult comparisons in the Rail business in Q1, as we've highlighted in the past, due to prior-year shipments against a large China project. That was \$3 million or \$4 million of operating income last year in Q1. We also, even though nickel prices improved in March for the quarter, they were still lower than they were a year ago.

We also had some incremental pension costs in the quarter that we assumed on the Infrastructure transaction. And we continue to spend \$2 million to \$3 million a quarter on consulting for Project Orion, which we did not incur last year. Those are some challenges year over year in the quarter.

We also recorded equity income from the Brand joint venture in Q1. You'll recall that we are recording that equity income one quarter in arrears. The amount that we recorded in Q1 was really the stub period in Q4 between when the deal closed and the end of the calendar year. That was about a loss of \$1 million due largely to seasonal issues during December as well as some one-time costs that were recorded between closing and the end of the year.

On chart 4, the key performance indicators for the quarter, revenues were \$513 million or up about 13% versus Q1 of last year. The Metals & Minerals business was up about 5%, and Industrial was about 13%. As expected, given the difficult year-over-year comp, the revenues in Rail were down about 20%.

Operating income was \$34 million. Again, that's adjusted. On a reported basis operating income was \$32 million. We had \$2 million of costs associated with the Infrastructure transaction which are tailing off. I suspect we may have some incremental costs in the second quarter, but that should be about it.

So the \$34 million of adjusted operating income was 5% higher than the same quarter last year. Metals & Minerals was roughly flat, Industrial was up about 5%, and Rail was up about 50%. Corporate costs were about \$2 million or \$3 million higher than the same quarter last year.

Our earnings per share was \$0.16 or up about 7%. To bridge operating income and EPS, interest expense was pretty much flat year over year. The tax rate was a bit lower at 24%, due to a few discrete items. We still expect the tax rate for the year to be 30% to 32%. Then of course we had the \$1 million loss in equity income. The return on capital figure was 6.4%; that's consistent with our plan as well. And as we go throughout the year, as we indicated, we expect ROIC to be between 7.5% and 8% for the full year of 2014.

Looking forward to the balance of the year, I'm on page 5, the outlook, as Dave mentioned, the operating performance is largely unchanged. Although our confidence level has increased. As you'll see in a minute we have increased our range of operating income for the year.

In terms of Metals & Minerals, if you look at the volume trends in the business and the price of nickel there's some potential upside there in the balance of the year. We have not assumed that in this current forecast.

We do think there's some risk as we navigate through Project Orion and more proactively address under-performing contracts it's possible that we could have some contract exit costs that are also not in the forecast. So we're looking at the risk-opportunity balance within Metals & Minerals to be fairly balanced.

Project Orion, we'll talk about that. We expect about \$3 million to \$5 million of benefit this year. So that's one of the drivers of the increase to the outlook for the balance of the year.

Industrial also is looking a bit stronger, steel prices are firming, natural gas prices are a bit higher. Those are both helpful. In terms of Brand, as we look at the outlook for cash earnings in the business for the balance of the year, it's very much consistent with the expectations that we had at the time the deal closed.

In terms of challenges for the balance of the year, the Rail projection has, I would say, an equal amount of risk and opportunity. As you may know, we have a sizable gap in revenue and profit year over year to fill from the expiration of the China contracts.

Free cash flow, the guidance for the year is still around zero. As you may recall, that's driven largely by significantly higher capital spending in the Metals and Minerals business. The cash flow from operations is actually up about 25% year over year.

I think we need to acknowledge that as we look through the balance of the year, even though we have a high degree of confidence in executing Project Orion, nonetheless it is a very broad program and there is some execution risk as we navigate through the balance of the year.

Then finally, we continue to lack the visibility that we'd like to have to the projected net income of Brand. As I said, we're very comfortable with the EBIDTA projections in the business but in terms of the effective tax rate, ongoing restructuring charges and perhaps some foreign exchange gains and losses, we just don't have the visibility to that going forward, so it's difficult for us to provide projections for net income for Brand.

Turning to slide 6, the outlook for the full year. These were the KPIs that we guided towards back in February, with the exception of operating income, our outlook has not changed.

Operating income guidance we have increased both the low and the high end of the range and also narrowed the range somewhat. We have been guiding on a full year basis to \$160 million to \$180 million and that range now is \$170 million to \$185 million. We would hope to provide EPS guidance in the next quarter, although at this point I think the right thing to do is focus on the operating income within Harsco, as well as cash flow and returns on capital.

Turning to the second quarter on page 7, the operating income guidance for Q2 is \$40 million to \$45 million. That excludes a charge that we'll take for phase 1 of Project Orion. So \$40 million to \$45 million on an excluding special item basis versus about \$49 million in Q2 of 2013.

The key reasons why earnings are expected to be slightly down from last year's second quarter, again, we have the final quarter of a negative comp on the China Rail contract. We also have pension costs related to the infrastructure business that we have assumed as part of the transaction that we did not have in the second quarter of last year.

Some contract exit costs that we talked about expecting in Q1 will now be in Q2. And then we also had some benefits in Q1 around corporate costs and expectation of some contract services and after market part revenue in Rail that was recorded in the first quarter.

So the segment outlook on page 8 really has not changed. This chart is very much the same as what we discussed back in February. So I won't go through it in detail. This just highlights the expectations for each of the segments in terms of revenues and operating income and the key drivers of those over the balance of the year.

So, let's turn to a more in depth discussion on Project Orion. I'm on page 9. I thought we should start by reminding everyone how we're looking at this business. You know, historically the Metals & Minerals business has been very focused on growth as opposed to return on capital. We've also had poor execution, and of course, we all know the global steel industry has weakened over time.

The two charts that we're showing here, I think, capture the essence of what we are trying to drive. The chart on the left indicates that of all of our customer sites where we provide services, approximately 60% of those we would categorize as acceptable performers. And that figure of 60%, certainly, is far too low.

Secondly, moving to the chart on the right, we look at historical free cash flow and return on capital and that free cash flow has averaged \$50 million to \$60 million over the past four years, for a \$1.4 billion revenue business. That, or course, is not acceptable. We also have return on capital of between 5% and 6%, that's also not acceptable. So, this just highlights and reminds everyone that we have a lot of work to do here, and that's why we are undertaking Project Orion.

On page 10, the overall objective of the project is to boost returns on capital and also to provide more consistent service to our customers. We started the program, you may recall, last July when we introduced this term, Simplification. So the first several months of the initiative were focused on simplifying the business.

Since that time, we've also added two additional areas of focus. We felt that looking at our process around bid and contract management, and how we approach underperforming sites, both needed to be overhauled. So, we've spent an awful lot of time the past several months building and redesigning those two core processes that, of course, have a very strong correlation to the performance of our business over time. So four areas of focus, primarily, in Project Orion. And I'll step through each of those four here in a minute.

Now, Dave touched on this a bit and questions have been asked rightly. So, what's different this time? Harsco Metals & Minerals has undertaken several restructuring programs in the past, and we are where we are. So, what's different this time?

I think there are many differences this time. Let me just step through them. I think it's important that you understand that this is a very different program from the historical programs.

First of all, there's been an awful lot of work done on mining the data and analyzing the data on a contract-by-contract basis. And all that data, and all that analysis, is now centrally located here at the divisional and the corporate office. In the past, that was spread out across sites and regions and countries. We simply had not done this level of analysis to understand what drives the business on a contract-by-contract basis in the past.

We've also had a very broad involvement of the internal team. This was not a few people sitting in an office figuring out how much cost we can take out. There were a lot of people involved, certainly within the Metals & Minerals business. Also the executive leadership team of Harsco was involved in the project.

We also brought in outside support. Initially on Simplification, and then a second firm we brought in to help us with the process redesign around the bid management process and the underperforming contracts process.

So, the focus was not simply on costs, but also on the core processes in the business, and we asked ourselves the question--is this regional, organizational structure optimal for the business? And we determined that it was not. So we are changing the structure of the organization, as well.

We've also initiated a number of pilot sites looking at applying some of these things that we've learned, and we've been very pleased with the early success of those pilots. And those certainly help underpin the projections that we'll talk about in a minute. Finally, we've built a dedicated project office to both drive the execution of Project Orion, as well as to monitor the progress against the milestones that we've established.

Just a few comments on the two elements of Simplification. First, looking at the initiatives above the site, we are shifting from a regional to a global functional structure. So we will have a global head of operations, a global head of commercial, and a global head of the bid-and-contract management process. We believe this will help us to prioritize the opportunities that we have, to leverage the knowledge that we have globally, and also to have a more consistent adherence to our best practices. We also expect, as part of the above-the-site reorganization, to realize a meaningful reduction in head count. And we'll be announcing that within a few weeks.

In terms of the at-the-site organization, as we've looked at the very disparate practices of our sites around the world, we've found a lot of inconsistency and competency gaps. The new organizations structure being more centralized will help to drive filling those gaps and will facilitate, what we'll call The Harsco Way. The Harsco Way will be a new set of standard operating guidelines and processes that will be driven throughout the globe.

I mentioned the initial pilots have showed a sizeable opportunity here. And the benefits include, not just head count reduction but also better maintenance, spending, and enhanced revenue opportunities.

So, chart 13 shows the financial benefits of the Simplification portion of Project Orion. We're executing this in two phases. Phase one starts now and will continue through the balance of 2014.

So as I mentioned, we will be taking a charge in this current quarter of \$7 million to \$10 million, a one-time charge, to effect phase 1. We believe that when we reach the run rate of savings from phase 1 will total \$20 million to \$25 million. We think we'll be at that run rate in the fourth quarter of this year and that the first full-year benefits will be 2015.

Phase 2 we expect to begin early in 2015. We expect an incremental \$10 million to \$20 million in benefits, realizing the run rates late in 2015, with 2016 being the first full year of those benefits. So in total we're looking at \$30 million to \$40 million of benefits. We're going to try to ring fence the costs in Q2 of 2014 and likely in Q1 of 2015. We're likely not going to be recording charges each and every quarter but we're hoping to do it in just those two discrete quarters.

Turning to slide 14, the process change as you might imagine, the bid-and-contract management process is really the life blood of this business. We're changing the way that's organized and structured.

So we now will have a dedicated central team that owns this process. The benchmarking that we've done of other companies that have similar profiles, that is the best-in-class model. They have a single dedicated centrally located team. That's what we're building.

In terms of the process, that central team will reach out to functional experts that we have around the globe. We'll have a very standardized stage-gate process that will be applied to every single opportunity, both in new contract as well as renewals. We're going to focus, not just on how attractive the project is, but we have a very good idea of how we assess the risk of achieving the returns that are proposed.

Then in terms of metrics, we will have a much better profile of metrics that we are tracking. Not just to approve the project, but also as the project is executed over time, continuing that audit process and ensuring that we are on track to deliver against those initial assumptions.

The underperforming contracts, another process change we're undertaking. We've constructed effectively a decision tree that we will use to step through the process of addressing each of the underperforming contracts that we have. We've begun that process. There are three or four

underperforming contracts that we're addressing as we speak. It's a very disciplined process. As you can see, on the right, it involves individuals from legal, commercial, from finance and from operations, and is going to be focused on cash flow.

So what's the net present value of exiting the contract versus staying the course, and points in between in terms of potentially renegotiating. We're going to approach this effectively in a triage type manner.

On 16, back in December at our Investor Day we provided some projections for the Metals & Minerals business out to 2016. We just wanted to update those.

So you can see that in terms of the EBIT margin, free cash flow and return on capital, what we projected for this business in 2016 has certainly improved by overlaying the benefits of Project Orion. We now expect EBIT margins to be about 300 basis points higher than we projected. We expect cash flow to be significantly higher, both driven by EBITDA improvement as well as by lower capital spending.

And then the return on capital, we think, will also increase significantly to 8% to 9%. Remember that's burdened by about \$500 million of goodwill. If you look at the return on capital in this business, excluding goodwill, we think we can get that to 12% to 13%.

On 17, this is a depiction of where we think we can take the portfolio of contracts. The chart on the left, this is the 60% of the contracts today that we think are acceptable. Collectively, we have about 7% return on capital at a site level, which excludes goodwill and corporate SG&A and so forth. We believe that in applying this program that site-level ROIC will go from 7% to 15% or 20% and the percentage of contracts that we view as acceptable will increase from 60% to about 80%.

So in summary, we're very committed to allocating capital to Metals & Minerals in a manner that's very closely linked with the success of Project Orion. We're going to focus on returns and cash flow as opposed to growth. Certainly there will be contracts that we exit and we will be investing in new contracts. There will be some growth in new contracts.

But the focus is going to be on returns. And the application of capital is going to be based on the team's ability to execute against what they've laid out. What we'll do going forward on future quarterly calls is provide you an update against the milestones that we've established around the size and the timing of the benefits, as well as how this contract churn and the improvement of the contract mix develops over time.

Finally, I just thought I'd bring this back to what this means for total Harsco. The chart shows targets in 2016 for EBITDA, return on capital and free cash flow. This is kind of the current projection for 2016 relative to what we had provided at our December Investor Day.

You can see, if you focus on the without acquisitions columns we're looking at a \$30+ million improvement in EBITDA, ROIC increasing about 2 points from what we had said, and free cash flow also increasing by \$30 million to \$40 million. These are the new kind of internal targets for where we think we can take the key financial measures of Harsco over the next 2 years.

Okay. So with that I will open the line up for questions for Dave, Dave and myself.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Your first question from the line of Jeff Hammond with KeyBanc Capital Markets. Your line is open.

Jeff Hammond - KeyBanc Capital Markets - Analyst

Hey. Good morning, guys.

Dave Everitt - Harsco Corp - Interim CEO

Hi, Jeff.

Nick Grasberger - Harsco Corp - President, COO & CFO

Good morning.

Jeff Hammond - KeyBanc Capital Markets - Analyst

A lot of great detail on the restructuring so congratulations. Just to be clear on a couple moving pieces on the outlook, I think earlier you talked about a point of margin improvement in metals. Is that still on track or do we look at a higher number with the savings? It's just a little bit apples, oranges with some of the corporate costs reallocation. I just wanted to understand if that is still a good thought.

Nick Grasberger - Harsco Corp - President, COO & CFO

Yes. If you take out the year-over-year noise and the change in the corporate cost allocations, so on a like-for-like basis the operating margins in Metals should be up 1% to 2%.

Jeff Hammond - KeyBanc Capital Markets - Analyst

Okay. Great. And then Nick, can you give us any sense of, you know, how this move in nickel prices impacts you guys and how big of an opportunity that is if these higher nickel prices hold?

Nick Grasberger - Harsco Corp - President, COO & CFO

Well, I think that if they would hold for the balance of the year it's probably a \$3 million or \$4 million opportunity if the demand for stainless steel stays where it is and nickel prices stay where they are. Because of the volatility of nickel prices we've chosen not to build that into our forecast, as I mentioned earlier. There is some other risks in the business as we execute Project Orion, specifically underperforming contracts. That would be roughly the size of the opportunity if nickel prices remain where they are.

Dave Martin - Harsco Corp - Director of IR

What we said in the past is a \$0.20 delta per pound in nickel translates to about 1% of operating income. That analysis still holds today.

Jeff Hammond - KeyBanc Capital Markets - Analyst

Okay. Great. And then are you actually seeing better order rates in your industrial business from, you know, higher steel, higher natural gas, or is that just something you'd expect going forward?

Nick Grasberger - *Harsco Corp - President, COO & CFO*

Certainly in the Air-X-Changer business we have been pleased with the order trends. In terms of the impact of steel, it's impact is really on the IKG grading process and that's more margin opportunity as opposed to a volume opportunity.

We did have a good first quarter in IKG. We had quite strong shipments, some of that I think was timing. But the outlook from a volume standpoint remains attractive for IKG.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

Great.

Operator

Next question from the line of Glenn Wortman with Sidoti & Company. Your line is open.

Glenn Wortman - *Sidoti & Company - Analyst*

Good morning, guys.

Nick Grasberger - *Harsco Corp - President, COO & CFO*

Hey, Glen.

Glenn Wortman - *Sidoti & Company - Analyst*

Is there a lot of variables in the target to savings resulting from the Metals & Minerals Improvement Plan. Can you provide any upside or downside risk to your target, say over the next several years?

Dave Everitt - *Harsco Corp - Interim CEO*

Yes. I think we feel that the upside and the downside risks are pretty balanced around that kind of \$30 million to \$40 million figure. You could say that there's additional opportunity as we roll out the Harsco Way at the sites, given what we've seen so far, which has been very encouraging. We're certainly starting with the sites that have the most room to improve.

We can't take those benefits and extrapolate them across all the under performing sites. None the less, there hopefully is some upside there.

At the same time we've assumed in phase 2 that we'll get some benefits from applying some technology that will enable some further efficiency, as well as the impact of some ongoing training and development. So those costs, although we're comfortable with them don't have the degree of confidence around them that say the phase 1 benefits do. I think that \$30 million to \$40 million range is a pretty good range. I would say one that we have a lot of confidence in.

Glenn Wortman - *Sidoti & Company - Analyst*

Okay. Just moving onto your revenue targets for Metals & Minerals through 2017, they range between \$1.3 and \$1.4 billion. Can you maybe break that down a little bit on some of your end-market assumptions? Has anything changed since your Analyst Day back in December? Does that still exclude the potential benefit from any new contract wins?



Dave Everitt - Harsco Corp - Interim CEO

So we do believe that the revenues will be in that range over the next three years or so. That's really the net of contracts that we exit; contracts that we renew and then some new contracts.

We really haven't assumed much of a change in volume on existing contracts in the business. We've not assumed any uplift, or a very modest uplift, I guess I should say, in nickel prices. So the revenue gains from manufactured products are fairly modest in our projections. But it's really, what you're really seeing in that range, is just the impact of this churn of improving the mix in the contracts over time.

Nick Grasberger - Harsco Corp - President, COO & CFO

I think it's fair to say that our focus is improving the business, not growing the business right now. We have to earn to right to grow.

We have a lot of the process improvements to make and so we're driving the organization for process improvements and more discipline and capital allocation, et cetera. That really says we're going to get some churn, but it's not a focus on growth until we get to the point where we can deliver this stuff on a regular basis.

Dave Everitt - Harsco Corp - Interim CEO

To be clear, in our somewhat reduced capital spending outlook for the business, we still have capital allocated to new contracts and into growth.

Glenn Wortman - Sidoti & Company - Analyst

On corporate expense, what should we be modelling there for the second quarter and what do you think the run rate would be in 3Q and beyond?

Dave Everitt - Harsco Corp - Interim CEO

I think for the full year we are looking 40ish in terms of corporate costs. I think they are a little higher in the first half than they are in the second. Maybe it's \$4 million or \$5 million lower in the second half of the year than the first half, something to that magnitude.

Glenn Wortman - Sidoti & Company - Analyst

And then last, can you remind us what your weighted average cost of capital is?

Nick Grasberger - Harsco Corp - President, COO & CFO

I think we just continue to assume it's around 10%.

Glenn Wortman - Sidoti & Company - Analyst

Thanks a lot for taking my questions.

Operator

Scott Graham with Jefferies.



Scott Graham - *Jefferies & Company - Analyst*

Good morning. Well done. Can you tell us, Nick, what the LST volumes were in the quarter?

Nick Grasberger - *Harsco Corp - President, COO & CFO*

Yes, I have that here. They were up about 5% versus Q1 of last year.

Scott Graham - *Jefferies & Company - Analyst*

That's all I needed, Nick, that was fine. Now, on the Rail, I think I modeled this a little bit wrong. When do the Rail comps ease up? What are you facing the next two quarters in the China Rail?

Nick Grasberger - *Harsco Corp - President, COO & CFO*

This is the last quarter, this current second quarter, so moving into Q3 we don't have that head wind year-over-year.

Scott Graham - *Jefferies & Company - Analyst*

On Brand business, the business leaders over there said, after you made your divestiture announcement, I think this is per your fourth quarter conference call, that the year could be a transition year for brand as well. I'm just kind of wondering what you feel that means for prior EBITDA assumptions. It sounds lower, obviously, but I mean how much lower, is your thinking?

Nick Grasberger - *Harsco Corp - President, COO & CFO*

Well, actually, the projection for the year for EBITDA is up. Certainly they are incurring restructuring costs and most of those benefits will certainly be realized in 2015 and beyond. But on a like-to-like basis from operations, let's say, the expectation is, and the projection and the plan for the business, and their tracking to it, is for EBITDA to be up this year.

It's a transition year, of course, because they are integrating two sizeable rather disparate businesses. So there is an awful lot of work going on at Brand right now. I'm recently on the Board, we have a board meeting next week on the audit committee, and I'm fairly close to the situation there. And I think there continues to be a very high degree of confidence in the management team and their plan to execute it. It is a bit frustrating that the visibility to net income is poor. But at the end of the day that is not the value driver, right, it's EBITDA and cash flow. And that continues to be on track.

Scott Graham - *Jefferies & Company - Analyst*

And the EBITDA up comment that you guys are making, that is on a pro forma basis for Brand? Or is that because of the acquisition of the infrastructure business.

Nick Grasberger - *Harsco Corp - President, COO & CFO*

No, that's on a pro forma basis. Pro forma basis EBITDA was \$300 million on a consolidated basis between the two companies. It'll be up this year.



Scott Graham - *Jefferies & Company - Analyst*

Got it. And my last question is do you, Nick, have the dollars for the contracts that you either exited or let expire in Metals & Minerals for the first quarter?

Nick Grasberger - *Harsco Corp - President, COO & CFO*

Yes, we do. I think Dave has them there.

Dave Martin - *Harsco Corp - Director of IR*

I'm sorry, Scott. What are you looking for? Revenues of the exit and lost contracts?

Scott Graham - *Jefferies & Company - Analyst*

That's correct.

Dave Everitt - *Harsco Corp - Interim CEO*

It was about \$15 million.

Scott Graham - *Jefferies & Company - Analyst*

\$15 million. Okay, thank you.

Operator

(Operator Instructions)

Jeff Hammond with Keybanc Capital Markets.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

Just a few follow ups here. On the Rail side, you put that in the challenge bucket. Is that kind of a timing discussion or is that you are still filling and finding orders to fill that \$30 million gap from China? And maybe just address how you are thinking about the margin performance there and if some of this favorable mix continues.

Nick Grasberger - *Harsco Corp - President, COO & CFO*

It's really the latter, the plan for the year was to fill that gap created by expiration of the China contract. We think they will but, to be fair, I think it is a challenge. That is their plan for the year and that is why I put it in the challenge bucket.

In terms of margins, the after market parts business, which is accretive to margins, has been growing somewhat faster than the volume in the equipment business, even though it's much smaller. So that has been accretive to margins. But I think we still look at this business over time as kind of a mid teens, low to mid teens, EBIT business.

Jeff Hammond - KeyBanc Capital Markets - Analyst

Great. Can you give us the acquisition impact on revenues in industrial?

Nick Grasberger - Harsco Corp - President, COO & CFO

Yes, I have, in terms of operating income, it was \$500,000 to \$1 million; revenues, I will say, \$4 million to \$5 million. I think the revenues are \$5 million, \$6 million.

Jeff Hammond - KeyBanc Capital Markets - Analyst

That's a pretty good run rate indicator of how to think about what the business is going to contribute?

Nick Grasberger - Harsco Corp - President, COO & CFO

The only thing I would add is the integration to the first quarter is going very well and we're pleased with the business model and I think it's going to turn out to be a great add for us.

Jeff Hammond - KeyBanc Capital Markets - Analyst

In capex you said there was some deferral, but is 240 still the right number to think about?

Nick Grasberger - Harsco Corp - President, COO & CFO

Yes, Jeff, it is.

Jeff Hammond - KeyBanc Capital Markets - Analyst

Finally, can you give us an update on your Metals & Minerals, JVs in China, and some of the new contracts that maybe are in that start-up mode and how they're ramping relative to expectations.

Nick Grasberger - Harsco Corp - President, COO & CFO

The largest one, Joint Venture Tisco has, this year, been performing quite well. We had assumed it would. It was still a significant ramp from where they had been performing. We're actually quite pleased with the performance there.

The others are still in ramp-up mode. As we look over the next two or three years in our modelling we expect a pretty significant improvement in the business from those contracts. There really is no reason now to believe that won't happen. I would say they're consistent with expectations at this point.

Jeff Hammond - KeyBanc Capital Markets - Analyst

Perfect. Thanks, guys.

Nick Grasberger - Harsco Corp - President, COO & CFO

Thank you.

Operator

Your next question comes from the line of Scott Graham with Jefferies. Your line is open.

Scott Graham - Jefferies & Company - Analyst

Hey, I wanted to ask a broader question about Orion. You know, the focus on the current sites is obviously very detailed, no question about it. The question that I would have is that with, Nick, you and I have talked about this, with so much of the steel complex having moved to Asia, what are your consultants telling you about that versus your offices being in North America and particularly in Europe?

Nick Grasberger - Harsco Corp - President, COO & CFO

We certainly have a strong direct presence in Asia. We have a sizable team there. We certainly would agree with you in terms of where the market is going.

We just talked about the very sizable wins that we've had and contracts the past few years in China, India and so forth, in the Middle East. Yes, I think our infrastructure is shifting increasingly to those regions to support the broader customer base.

Dave Everitt - Harsco Corp - Interim CEO

The piece I'd add to it, is that this new organization structure, I think is going to enable us to take the good practices that we have elsewhere in the world and get them embedded in these new operations faster and at a more consistent way, which in the past would have been more ad hoc with a regional focus. I think it's the right time for this because as we're starting up the right way. We talked about, as Nick mentioned, this allows us to embed the proper management of those contracts early in the phase rather than later. I think it's a win-win from that stand point.

Nick Grasberger - Harsco Corp - President, COO & CFO

Just to be clear, this shift from a regional to a more centralized structure doesn't mean we're pulling people out of the regions. We're certainly not.

Scott Graham - Jefferies & Company - Analyst

Let me ask just a quick piggy-back question onto that, if I may. The rise in EBIT's margin that you're expecting in the business versus the rise in ROIC you're expecting, it's a little bit of a lag on the ROIC side, and that was the some of the thrust of my question. Are you guys thinking that you need offices, you know, to be on the ground more in Asia and that's the reason why maybe you have more capital dollars, whether it's this year or next year or what have you, to spend to get there?

Nick Grasberger - Harsco Corp - President, COO & CFO

Well, we agree we need a larger presence. We really don't have any capital in this plan allocated to building that out.

The issue, and why it appears to be a lag is simply that we have \$500 million of goodwill in this business, so it's a very sticky number. It takes a while to move that figure. You need a lot of higher earnings to move that north.

Perhaps the better metric, the one I like to look at, is the EBITDA minus CapEx margin. That's growing significantly.

If you think about EBITDA minus CapEx in 2014, the margin is probably 3%. If we achieve this plan in 2016 that margin will be 10%. So I think over time we should focus perhaps more on EBITDA minus CapEx as a margin and how we're going to drive it, as opposed to simply EBIT margin.

Scott Graham - *Jefferies & Company - Analyst*

Understood. Thank you all.

Operator

And we have to further questions in queue. I'll turn the call back over to the presenters.

Nick Grasberger - *Harsco Corp - President, COO & CFO*

Good.

Dave Martin - *Harsco Corp - Director of IR*

Well, thank you for joining us today. If you have any further questions feel free to reach out to us via e-mail or on the phone this afternoon. Thank you.

Operator

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

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