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PRESENTATION

Operator

Good day. My name is Carmen, and I will be your conference operator today. At this time, I would like to welcome everyone to the Harsco Corporation third-quarter release conference call.

(Operator Instructions)

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I would like to introduce Mr. David Martin, Director of Investor Relations. Mr. Martin, you may begin.

David Martin - *Harsco Corporation - Director of IR*

Thank you, Carmen. And welcome to everyone joining us today.

As Carmen said, I'm Dave Martin, Director of Investor Relations at Harsco. With me today is Nick Grasberger, our President and Chief Executive Officer. This morning we will discuss our results for the third quarter of 2014 and our outlook for the remainder of the year, as well as provide you an update on Project Orion. And then we will take your questions.

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

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

Thirdly, 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, please see the risk factors section in our most recent 10-K and 10-Q, as well as in other -- our other SEC filings. The Company undertakes no obligation to revise or update any forward-looking statements.

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 the back of our presentation.

Now I'll turn the call over to Nick Grasberger, our President and CEO.

Nick Grasberger - *Harsco Corporation - President & CEO*

Thank you, Dave. Good morning, everyone. I'm on Page 2 of the slide deck. I'll begin with a comment about our leadership team. A few weeks ago, we announced the appointment of Peter Minan as Harsco's CFO, completing the build-out of our senior executive team. Pete had a very distinguished career at KPMG, including leadership roles for both the Washington, DC and US national audit practices. And has extensive and relevant experience working closely with leading multinational public companies. I have no doubt Pete will provide the leadership and judgment necessary to support the transformation of Harsco in the coming years. He'll officially join next week, but Pete has already displayed the talent and energy to quickly learn our Business and contribute immediately.

Turning to our financial results, the third quarter developed largely as we expected. Strong sales of high margin after-market parts in our Rail business and lower corporate costs offset modest profit shortfalls in Metals & Minerals and the grating business in our Industrial division.

Adjusted EPS grew 60% versus Q3 of 2013. Free cash flow exceeded $60 million. And return on capital for the trailing12 months was 7.2%, about 150 basis points above last year's figure. Dave will step through the specifics of Q3 in a minute.

Our initial guidance for the year indicated profits for the first half of the year would be slightly lower than the first half of 2013, while second-half profits would be above those of last year. That continues to be the case. Our current forecast projects both operating income and EPS to improve at a double digit rate in the second half of this year. We have, however, reduced our outlook for the fourth quarter, due largely to timing issues on Rail shipments and asset sales in the Industrial division, foreign exchange effects, and higher consulting costs at corporate to support Project Orion in Metals & Minerals.

The profit outlook for M&M has also weakened in Q4, based on the performance of a small handful of customer contracts. As we've discussed previously, it is difficult to predict with much certainty the timing of the exit or renegotiation of underperforming contracts. We'll speak further about the progress against the key initiatives of Project Orion a bit later, but we do expect the pace of contract actions and restructuring charges to increase significantly in the fourth quarter.

Overall, we are pleased with the trends in each of our businesses, and also with those in our Brand Energy joint venture, and believe we will exit 2014 with significant momentum. As we look ahead to 2015, we are confident that operating income and EPS will improve at moderate double digit rates, and we expect to deliver notable increases in both free cash flow and return on capital, due to the benefits of Project Orion, the backlog of Rail orders, and the macro trends that are supporting both our Industrial businesses and the Brand Energy joint venture.

I'll now turn the call back over to Dave.

David Martin - *Harsco Corporation - Director of IR*

Thanks, Nick.

And if you would turn to Slide 3, this slide highlights some of the key points for the third quarter. Starting with the fact that third quarter adjusted operating income was $49 million in the quarter versus our August guidance of $43 million to $48 million, in addition to that, our adjusted operating income in the quarter surpassed prior year levels by about 19%.

Performance in both our Rail business and at corporate was better than we expected in the quarter. In Rail, similar to the second quarter of this year, the business did benefit from favorable mix of higher margin parts and service revenues, and much of the benefit in the third quarter was pulled forward from the fourth quarter, or the current quarter. At corporate, the story was somewhat similar. Costs were lower in the third quarter, largely because of timing.

In our Metals & Minerals business, net contract outcomes were again accretive to operating income, and this was true for the fourth consecutive quarter. And the business did achieve its best result of the year, which we think illustrates the progress we are making in this business.

In our Industrial segment, our heat exchanger, as well at our commercial boiler business continue to perform quite well. Hammco results were consistent with the prior quarters of this year. And Hammco, again, contributed about $1 million to operating income in the quarter. And these positives were partially offset by challenges in our industrial grating business, which we have talked about in the past and we are hopeful will ease a bit in 2015. ROIC reached, as Nick said, 7.2% in the quarter. And this compares favorably to 6% ROIC in full year 2013.

Our joint venture with CD&R, our Brand joint venture, did contribute positively to results this year -- I'm sorry, this quarter. The equity contribution was $5 million. And this puts year-to-date equity contributions from Brand in positive territory, or at approximately $1 million, despite significant restructuring costs at the joint venture.

The only other item I would mention on this slide is related to free cash flow. Free cash flow was ahead of our expectations in the quarter. And this was mainly due to contract advances in our Rail business, as well as under-spending of capital. Year to date our capital spending has totaled just over $130 million, which is well below what we forecasted earlier in the year.

And we've now reduced our capital budget by more than $50 million versus what we said in August, with most of that change coming in the Metals & Minerals business. And we're now forecasting capital spending for the entire Company at about $190 million.

If you turn to Slide 4, here we show some of our key performance indicators. Firstly on revenues, revenues in the third quarter were $526 million. This represented an increase of $29 million year over year, and each of our business segments reported an increase in revenues versus the prior year.

The largest increase was in Metals & Minerals, where revenues grew approximately 12%, and this was driven first by volume improvements. Our LSTs were up just over 2%. Also we saw a somewhat meaningful increase in our byproduct shipments in the quarter. And also M&M benefited from higher nickel prices, as nickel prices rose almost $2 a pound year over year.

In our Industrial business, revenues improved about $10 million, and this was mainly because of the Hammco acquisition, while in Rail, revenues increased $7 million, primarily due to higher spare part sales. On operating income, adjusted operating income again was $49 million. This compares favorably to $41 million in the prior year. The majority of that improvement was driven by our Rail business. Rail operating income increased $7 million because of contributions from higher margin parts and service sales.

Our Industrial business did report a modest improvement in operating income. OI in that business increased $1 million, again mainly because of Hammco. Elsewhere in our Industrial business, year-over-year improvements in our heat exchanger business, as well as our commercial boiler business were largely offset by reduced performance at our industrial grating business. Lastly in our M&M business, operating income was essentially stable, as revenue improvements were offset by higher maintenance and equipment costs, as well as site exits year over year.

All of these moving parts did translate to higher margins in the quarter. Our operating margin was 9.2% versus 8.2%, excluding Infrastructure, in the prior year. On an EPS basis, adjusted EPS was $0.32. This compares to our August guidance of $0.26 to $0.31. And was well above prior-year levels, which was $0.20. And it's important to note the Brand joint venture contributed about $0.04 to EPS this quarter.

On free cash flow, free cash flow increased about 25% year over year to $65 million in the quarter. And the primary contributors here again were lower Cap Ex, as well as contract advances.

Turning to Slide 5 and our 2014 outlook, let me make four, five, six comments on this slide. Starting with our Industrial business, which continues to experience favorable volume growth for heat exchangers and commercial boilers. This should drive, or is expected to drive both an improvement in revenues and operating income in the quarter. On Rail, this business continues to perform in line with plan, and there's essentially no change in our outlook for this business.

Thirdly, on Metals & Minerals, higher LSTs, as well as nickel prices are expected to drive a modest improvement in revenues in the year, and on Project Orion our benefits for the year are unchanged. We continue to expect Project Orion benefits between $5 million and $7 million for the year, and this includes benefits realized in the third quarter of approximately $2.5 million.

Onto our Brand joint venture, our guidance for the year is now equity income of $5 million to $7 million. This compares to prior guidance of between $5 million and $10 million previously. And the reduction of the high end, if you would, is largely due to increased restructuring costs at the business.

Coming back to M&M quickly, one item I overlooked and should have mentioned as far as the positives in M&M, and are highlighted under the challenges section on this slide is that these positives again are being offset by a number of items, some of which we have mentioned in the past. These items would include slower new site ramp-ups, site exits, as well as some bad debt expenses that we recorded earlier in the year. And in total in the M&M business now, we're expecting operating income to be similar to what it was in 2013 after considering these items, as well as increased maintenance and the impacts of foreign exchange on M&M.

Regarding other challenges, I think it's worth me noting, as was mentioned in the press release and by Nick, we are anticipating fewer asset sales gains this year because of likely delays in selling a couple properties. We do continue to believe firmly that these transactions will take place, but they are now expected in early 2015 as opposed to late this year. And lastly on free cash flow, our free cash flow outlook is unchanged at $35 million to $65 million, as lower cash flow from operations is offset by lower Cap Ex.

Turning to Slide 6, and our outlook details for the year, on operating income, our range is lowered to $152 million to $157 million. This compares to prior guidance of $170 million to $180 million, and compares to adjusted operating income in 2013 of $152 million. So in total, our operating income guidance has been lowered by approximately $20 million, and I think it's important to reemphasize, or emphasize further, that approximately half of this change is attributable to what I would call timing issues, as well as foreign exchange.

These timing issues are things like asset sales delays, Rail shipment timing, as well as added consulting fees to support the acceleration of Project Orion in M&M. The remainder of the change is primarily driven by our outlook for our industrial grating business, as well as maintenance costs in the ramp schedule at a number of sites in Metals & Minerals.

On earnings per share, our guidance is now $0.76 to $0.80. This compares to prior guidance of $0.92 to $1.04, and prior-year adjusted EPS of $0.87. It's important to note that this forecast does now include a higher effective tax rate. We're now assuming a range of between 34% and 36% versus 31% to 33% back in August. And this change does have approximately a $0.04 EPS impact on our guidance. It's also worth noting that the year-over-year EPS comparison is complicated by a number of items: first and foremost the higher tax rate I mentioned, and also the CD&R joint venture unit adjustment, which was not present last year.

Turning to Slide 7 and the specifics on our outlook for the fourth quarter, our guidance for adjusted operating income is $28 million to $33 million versus $30 million in the prior-year quarter. And we're expecting a range of adjusted earnings per share of between $0.11 and $0.15. This compares to $0.20 in the fourth quarter of 2013. And again, here I think it's important for me to emphasize that the year-over-year comparison is complicated by a much higher effective tax rate, and we're assuming a tax rate in the mid-40%s for the fourth quarter.

As far as key year-over-year changes that impact operating income for each of our segments, they are noted on Slide 7. Let me just highlight a few of those. In Metals & Minerals, Project Orion benefits are expected to be between $3 million and $4 million, and increased nickel prices, in combination with Project Orion benefits should result in a modest improvement in operating income in the quarter.

For our Industrial business, the inclusion of Hammco, as well as volume growth, is expected to also drive an improvement in results here. Meanwhile, in our Rail business, because of less favorable mix and the timing issues we talked about earlier, the Rail business is likely going to have lower results year over year versus last year.

And then on the corporate side, despite what I said earlier about higher consulting fees to support Project Orion, corporate costs will be down, or expected to be modestly lower year over year, because of reduced consulting costs. And lastly on the fourth quarter, as was stated in our press release and Nick referred to earlier, you should expect a number of special items in the fourth quarter related to Phase II of Project Orion and the initiatives underway in that business.

And then turning to Slide 8, if you would, most of this I've covered. But again, it's worth noting that the changes to our outlook on this page, which are mainly to the Metals & Minerals business and to our Industrial forecast. In M&M, we're now forecasting flat operating earnings versus a modest increase previously. And in our Industrial business, we're now pointing to operating income growth of in the high single digits to low double digits to low double digits previously, and again, that's mainly driven by our outlook for the industrial grating business.

Lastly on this slide, for modeling purposes let me note that the added consulting fees that were mentioned, as well as the impacts of fewer asset sales, would show up on the corporate line. So, let me stop there and turn it back over to Nick to discuss Project Orion and provide his summary thoughts, before we take your questions.

Nick Grasberger - *Harsco Corporation - President & CEO*

Thank you, Dave.

I'm on Slide 9. We believe we're making respectable progress towards delivering against our Project Orion goals that we established last spring. You may recall that we're focused on four principal initiatives. In terms of the above-the-site improvements, the new global functional organization is in place, led by Rick Lundgren. Rick is doing a tremendous job of leading the business in a very disciplined, decisive manner, and is driven by our goal of generating returns above our cost of capital. I look forward to introducing Rick to many of our investors over the next few months.

The headcount reductions in Phase I of the program are largely complete, both above the site and at the site. But of greater importance are the new operational standards that we've adopted and are rolling out globally. We call these the Harsco Way, and are convinced that the disciplined adoption of these standards at each customer site will make step-change improvements in both our cost structure and the consistent delivery of the value-added services to our customers. The estimated benefits of Phase I of the program are approximately $25 million on an annualized basis.

The new bid-and-contract management function is also in place, and is modeled after the best-in-class process identified through our strategic planning exercise last year. The bid-and-contract management team is independent of our commercial team, but staffed with experts from within each function, including commercial, operations, finance, legal, and engineering. They have established new contractual standards for commercial terms, financial metrics, and legal provisions, and are charged with vetting and either approving or rejecting contract proposals, and then tracking the performance of the executed contracts over time. We're confident that this team and this process will lead to a much lower percentage of underperforming contracts in the future.

In terms of underperforming sites, we have increased resources to the group managing our so-called triage process for addressing the weakest performing contracts. Overall, 25% of the original underperforming contracts are now generating acceptable returns, while a few additional contracts have moved to underperforming status.

Our approach to addressing underperforming contracts continues to be driven by economics. If operational improvements and/or changes in contract terms provide a better overall return than exiting the contract, we will continue. Otherwise, we will exit.

To no one's surprise, this exercise takes time, and customer relationships play an important role in these discussions. As indicated earlier, we expect a resolution of a number of these discussions to occur this quarter. And as you saw in the second quarter, the short-term effects can be challenging.

So in summary, our business focus and strategy have not changed. We are progressing down the somewhat lengthy path of fixing the M&M business and generating returns above our cost of capital in that division. We are investing further in the growth of Rail and Industrial, and are very encouraged by the opportunities we see, and the execution capabilities of our leadership teams.

At the same time, we are upgrading the talent and building better processes in the corporate functions that support our businesses. But perhaps of greatest importance, we now have a complete high caliber executive team in place to execute our strategy and reshape our portfolio over time. As noted earlier, we are excited and optimistic about our prospects in 2015, and believe our financial performance will demonstrate a meaningful step towards achieving our long-term, targets of doubling ROIC and EBITDA minus CapEx.

Dave and I are now happy to entertain questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

The first question from Jeff Hammond of KeyBanc.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

Good morning, guys.

Nick Grasberger - *Harsco Corporation - President & CEO*

Hi, Jeff.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

So just as it relates to, I guess you cited for the fourth quarter lower guide, a couple of things. One, exit costs, and two, kinds of Rail timing and mix. Are you able to quantify those two items?

Nick Grasberger - *Harsco Corporation - President & CEO*

Yes, let me just step through -- I think Dave mentioned that over half of the reduction in guidance is due to those type of issues. First of all, we had assumed in the prior forecast that a few grinders in the Rail business, which each carry a few million dollars of profit, would be booked in Q4. It's now looking as though those will occur in Q1. It could happen in Q4, although we're assuming they'll move into Q1.

We've also spent probably an additional $2 million or so on consulting costs supporting Phase II of Project Orion. We'd assumed in the previous forecast that that consulting support would end in the summer. And we now believe the right thing to do is for it to continue through the balance of the year.

I think we mentioned FX as well. The impact of FX has been a few million dollars. And then we also, as part of the consolidation of our four manufacturing facilities in Tulsa, in the Air-X business into one, we assumed that we would sell one of the principal facilities there that would have produced a, I don't know, $3 million, $4 million, $5 million gain, I believe.

So those items collectively, some of them are timing, and some of them are more one-time in nature, for example, the consulting fees. So I think if you look at those in total, that that's well over -- or a bit over $10 million or so of change in income for Q4.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

Okay. So just -- are there exit costs that hit 4Q as well? I don't know if you mentioned that.

Nick Grasberger - *Harsco Corporation - President & CEO*

No. The exit costs, to the extent we have them, and we likely will, will be put to the side as special items in Q4.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

So the headwinds in Metals & Minerals relative to your forecast before is some FX, some of these elevated consulting, and then a little bit weaker demand?

Nick Grasberger - *Harsco Corporation - President & CEO*

I wouldn't say demand. There are really three contracts that we assumed would ramp up in the second half of the year, and those are simply delayed. They were high margin contracts. And so we'll look at those as having an impact in 2015.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

What's behind the delay? And is there any reason they don't get started by 2015?

Nick Grasberger - *Harsco Corporation - President & CEO*

Well, the reasons vary. They are not in the US. They're in Europe and in Asia. The reasons are myriad. I would say in a few cases it's quite likely that those contracts will ramp up in 2015.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

Okay. Because you made the comment, and maybe you can give us more clarity on what you mean by moderate double digits op income growth. It just seems like if you look to 2015, and we can debate the macro, but it seems like you have a lot of one-time costs, kind of these consulting fees that should roll off, that haven't been excluded. And then you have, I think we were modeling $13 million of incremental Project Orion savings. That right there gets you to your moderate, I guess, low, low double digit op income growth. And on an EPS side, I would think that that number would be a lot bigger, just based on the JV income ramping.

Nick Grasberger - *Harsco Corporation - President & CEO*

Yes, that's true. Your latter comment certainly is true. In terms of operating income, you're right. I mean, there are some tailwinds we'll have on the cost side headed into 2015. We also expect Rail and Industrial certainly to grow year over year. And kind of the piece that's not yet quite quantified on 2015 is, which contracts we are going to exit and which we will continue, and therefore, what's the revenue and income impact of those? We certainly expect the M&M business to be up double digits, moderate plus.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

But I'm assuming any contracts that you exit are going to be less favorable from a profit standpoint?

Nick Grasberger - *Harsco Corporation - President & CEO*

Yes, certainly there are many that are profitable but below the threshold of full returns. So we -- yes.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

So the headwind is, you're exiting contracts that are below your return on capital hurdle rates, but have some margin to them?

Nick Grasberger - *Harsco Corporation - President & CEO*

That's correct, yes.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

Okay. Thanks, guys.

Operator

Your next question is from the line of Glenn Wortman with Sidoti and Company.

Glenn Wortman - *Sidoti & Company - Analyst*

First, what's driving the higher tax rate forecast for 4Q? And then how should we think about modeling that for next year?

Nick Grasberger - *Harsco Corporation - President & CEO*

The higher tax rate in the fourth quarter's really all about the geography of earnings. And in some cases, having in-country losses that are not benefited from a tax standpoint. I think as we look forward, I think we previously guided the tax rate in kind of the low to mid-30%s. I think we see that -- we still view that as valid going into the 2015.

Glenn Wortman - *Sidoti & Company - Analyst*

Okay. And these consulting costs for the M&M business, are those hitting the M&M line or is that --

Nick Grasberger - *Harsco Corporation - President & CEO*

No, they're corporate. They're corporate.

Glenn Wortman - *Sidoti & Company - Analyst*

Okay. So it sounds like corporate costs should come in this year around $43 million? Is that right, and how should we think about that going forward?

David Martin - *Harsco Corporation - Director of IR*

Glenn, I think what we've said in the past is low $40 millions. So given what we've said today about some of the pressures on that line for the fourth quarter, yes, it should be somewhat higher than that.

Glenn Wortman - *Sidoti & Company - Analyst*

Okay. And then just moving on to the Rail business 4Q. I think based on your comments, it looks like revenue for that business could be down about 25% year over year in the fourth quarter. It sounds like some shipments were pulled forward, some were pushed out. How are you thinking about that business heading into 2015? It sounds like (multiple speakers)

Nick Grasberger - *Harsco Corporation - President & CEO*

Let's just talk about 2014 first. Coming into 2014, we had a $9 million earnings gap from the expiration of that large contract in China. And we were concerned about our ability to fill that. That's a pretty big gap for that business. And in fact, we filled it and went beyond. So that business will grow 8% or 9% in earnings this year despite that gap. And a lot of that has come from after-market parts, where we did not have much of a presence a couple years ago, and now it's a significant part of the business with very high margins. And that trend should continue into 2015.

And then in 2015, I think as we've disclosed previously, we will begin to ship later in the year against the Swiss Rail contract, which is sizable. And there are now two parts to that. So a few hundred million dollars of revenue over 2015, 2016, and 2017. But I would say even beyond that, the traction that we've gained outside the US in our Rail business is really quite impressive. We now have a very strong presence, and not just as evidenced by winning the Swiss tenders, but other businesses we've been winning.

So I think we truly now view the Rail business as an international business. We couldn't have said that a couple years ago. It was a US business plus a big China contract, right? So we feel very good about the Rail business. And as we've indicated before, we continue to track some businesses in the space that we think might be a good fit into our Rail business through an acquisition. So we're very focused on growing that business.

Glenn Wortman - *Sidoti & Company - Analyst*

Okay. And then just one more, moving onto Metals & Minerals. You maintained your long-term targets. But can you maybe update us on how you think the margin improvement will progress, say, each year for the next several years?

Nick Grasberger - *Harsco Corporation - President & CEO*

Yes. I would think the margins, the operating margins, should be up between 1 and 2 points next year. And the same with return on capital, headed towards, I think, we're looking at a return on capital in two or three years at 8% or 9%. Of course, not where we want to go ultimately. But that's what we think is achievable in the next couple of years.

Glenn Wortman - *Sidoti & Company - Analyst*

Okay.

Nick Grasberger - *Harsco Corporation - President & CEO*

But there's no question that 2015 relative to 2014 should be a quite good year for M&M.

Glenn Wortman - *Sidoti & Company - Analyst*

Okay. Thanks a lot for taking my questions.

Operator

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

Scott Graham - *Jefferies & Company - Analyst*

Good morning. I want to maybe go a little further on Jeff's question because it seems that when you add the numbers up, the outlook for 2015 seems conservative. First maybe I would ask, when you say moderate double digit, is that 12%? Is that 15%? I would have assumed you would say teens. Is that 12%? Is that a number you're thinking? Is that what resonates?

Nick Grasberger - *Harsco Corporation - President & CEO*

It's higher than 12%.

Scott Graham - *Jefferies & Company - Analyst*

But not 20%?

Nick Grasberger - *Harsco Corporation - President & CEO*

It might be 20%. Look, we've not yet put our budget together for the whole year. What we simply are trying to convey, which may well have been clear before, was that let's not extrapolate this fourth quarter into 2015, right? We still expect 2015 to be a very strong year financially, and really across all of the metrics. So we're not intending to provide specific guidance at this point. We'll do that in February. We're just trying to convey is that nothing's changed in terms of our rather sanguine view on 2015 financially.

Scott Graham - *Jefferies & Company - Analyst*

Fair enough. The asset sales, I guess I was a little bit surprised that that was part of the guidance. What was the dollars that you were assuming would kind of ring through in the fourth quarter for asset sales?

Nick Grasberger - *Harsco Corporation - President & CEO*

Yes, it was really -- again, there's some property in Mexico. There's this facility that I referenced in Tulsa. Both in the Industrial division. I think between the two of them, it was $3 million or $4 million.

Scott Graham - *Jefferies & Company - Analyst*

Okay. Thank you. On the LSTs, do you have that number? I didn't see it, the percent change in LSTs?

David Martin - *Harsco Corporation - Director of IR*

Year over year was 2.2%.

Scott Graham - *Jefferies & Company - Analyst*

And pricing was up there as well, right?

David Martin - *Harsco Corporation - Director of IR*

Nickel price, yes.

Scott Graham - *Jefferies & Company - Analyst*

Yes. The contract exits, the revenues, could you tell us that?

David Martin - *Harsco Corporation - Director of IR*

Yes, Scott. Sure. On the exits from underperforming contracts and contracts we didn't renew, the combined impact, revenue impact was approximately $16 million.

Scott Graham - *Jefferies & Company - Analyst*

$16 million, okay. I guess the last question would be kind of more on what your customers are saying. Obviously, there's been a gap-down in commodity prices. And I know there's a little bit of an oil impact on your Industrial business, but more so on the steel side where the prospect for steel price increases, certainly in the intermediate term, seems to be dimmer. I'm wondering how that translates into their spending. What are your customers saying now in steel as you are exiting the year?

Nick Grasberger - *Harsco Corporation - President & CEO*

I think that we view that impact, the macro impact, on the business as much more benign than what we're doing in Project Orion. I think that it's for us, the incremental impact of a 1 point change in LST, let's say, is much less impactful than the process that we're navigating through in Orion. We don't have assumed, for example, in 2015 any significant change in kind of the core volume in the business based on what's happening in the steel industry.

David Martin - *Harsco Corporation - Director of IR*

Broadly speaking, the geography of our M&M business is very diverse. We are in 30-plus-odd countries. Near-term perspective from our customers can vary quite a bit. I think if you look at our performance this year, LST performance if you would, the best comps tend to be in places like Europe and China. And I don't think there's really been much of a change in the outlook from our customers recently.

Scott Graham - *Jefferies & Company - Analyst*

Got it, thank you. My last question is just more of a housekeeper. Is there anything we should be reading into the fourth quarter tax rate that kind of moves you away from that sort of low 30%s rate that I think we were looking at previously for 2015?

Nick Grasberger - *Harsco Corporation - President & CEO*

I think it's fair to assume low 30%s, maybe 33%, 34%. But no, I don't think the long-term view has changed.

Scott Graham - *Jefferies & Company - Analyst*

Very good. Thanks, guys.

Nick Grasberger - *Harsco Corporation - President & CEO*

Thank you.

Operator

Your next question comes from the line of Rob Norfleet with Alembic Global.

Nick Chen - *Alembic Global - Analyst*

This is actually Nick Chen for Rob Norfleet this morning. Thanks for taking my call. You touched on it a little bit earlier, but I was hoping we could dig a little deeper into the status of underperforming contracts in the M&M segment. Specifically, just what percentage are you still trying to renegotiate, and how many remain in a loss position?

Nick Grasberger - *Harsco Corporation - President & CEO*

Yes. Well, in terms of in a loss position, I'm going to say there are probably 8 to 10 that actually have negative gross profit. Obviously, we have a much higher number that are below our threshold for what's an acceptable return. As I indicated earlier, the original list of underperformers based on a return threshold has come down nicely, both due to operational issues, and in some cases contractual issues. And also some that were underperforming because they were early in their stage of ramping up and now they are. But we are very actively, this triage team that we referred to before, we're putting a lot of resources against specific contracts. There are 13 or 14 contracts that are in that triage process as we speak.

Nick Chen - *Alembic Global - Analyst*

Great. And just one last question, and I'll get back into queue. In regard to Industrial and Rail, you've said these are both markets where you want to grow through acquisition. Can you discuss any potential opportunities you're seeing? And is pricing right now rational, or have the multiples just become too pricy?

Nick Grasberger - *Harsco Corporation - President & CEO*

No, there's nothing specific that I would comment on right now. And yes, there's no question in many markets it's -- where the prices are would not be viewed as attractive to us right now.

Nick Chen - *Alembic Global - Analyst*

All right, great. Thanks so much, guys.

Operator

Your next question is from the line of Bryan Carlson with Atlantic Investment.

Bryan Carlson - *Atlantic Investment - Analyst*

Good morning. Can you guys hear me okay?

Nick Grasberger - *Harsco Corporation - President & CEO*

Yes.

Bryan Carlson - *Atlantic Investment - Analyst*

So I just wanted to dig in on the underperforming contracts again a little bit here. I think that you originally outlined that 15% of the contracts that you had were underperforming. If there are 170 sites, that's like 25-odd contracts. Is that all fair?

David Martin - *Harsco Corporation - Director of IR*

We originally said 40%, Bryan.

Nick Grasberger - *Harsco Corporation - President & CEO*

Yes, back on the Investor Day last year when we began to look at this, we estimated 40%, Since that time, we've actually changed the definition of what is an underperforming contract. I think that number's still about the same.

Bryan Carlson - *Atlantic Investment - Analyst*

So something more like --

Nick Grasberger - *Harsco Corporation - President & CEO*

I think what you're referring to, Bryan, is more the portion of that 40% is the sites or the contracts that we can go after aggressively, meaning some are ramping down, some are ramping up. It's the other bucket, which we said was about 20%, which is the target.

Bryan Carlson - *Atlantic Investment - Analyst*

That's the target that you're actually trying to address? I mean, obviously ramp down, you're just letting that happen. Ramp up, you're trying to accelerate it, but you're letting that happen as well. So to clarify, instead of 26, that number should be more like 35 that you're really targeting and trying to triage? You're going to do something about these contracts, is that fair?

Nick Grasberger - *Harsco Corporation - President & CEO*

That's fair.

Bryan Carlson - *Atlantic Investment - Analyst*

Of those 35, you're saying maybe 8 to 10 are negative gross profit. I assume all of those are in that 35?

Nick Grasberger - *Harsco Corporation - President & CEO*

Yes.

Bryan Carlson - *Atlantic Investment - Analyst*

Okay. So that leaves something like 25 that really are sort of money-makers, but not making the cost of capital you want to have them at. That group, what is the assumption that you have for dealing with contracts embedded in the sort of modest, or the low double digit EPS growth and operating profit that you've outlined next year? Because it seems like to me, I mean, the benefit from mix you guys have outlined as $50 million to $60 million over like a three-year period. Orion is $35 million to $40 million benefit. There's offsetting churn and other costs, I think are like $25 million.

It's hard to have -- to hear you say Orion is up, Brand is up next year, the Rail/Industrial businesses will be better next year, and understand why the operating margin increases, or the operating profit increase is so modest, and the EPS increase is so modest. Brand and lower tax should result in much better numbers, I guess. Maybe my issue --

Nick Grasberger - *Harsco Corporation - President & CEO*

You're talking about 2015 or 2014?

Bryan Carlson - *Atlantic Investment - Analyst*

Yes, 2015. Maybe my issue is not understanding how much of the --sort of the, what you would call underperforming contracts are going to be removed. So can you just dive in on that a little bit?

Nick Grasberger - *Harsco Corporation - President & CEO*

First of all, I didn't use the word modest. I think we said moderate in terms of what we expect the increase to be in earnings next year. Clearly, with respect to EPS, as Jeff noted, because of a full year of Brand positive earns, whereas the first two quarters this year we booked negative income, the impact of that on EPS will be pretty significant next year.

We'll see significant gains in EPS next year. But quite frankly, we're not yet ready to talk specifically about 2015. We're just talking directional here and indicating that we feel quite confident in what we might view as kind of a step change in terms of performance of this Company financially in 2015, for all the reasons that we've discussed. And you just mentioned a few of them as well.

So -- but you're right. In our three-year model that yielded the long-term return in cash flow targets, we had assumed a significant lift from the addressing of these underperforming contracts. And that remains the case. We just have not yet built that 2015 plan that make the assumption of how many of those are going to be successfully addressed and what the impact will be in 2015. That's what we'll do in the budgeting process, which will begin here soon.

Bryan Carlson - *Atlantic Investment - Analyst*

I know you had some sort of trial projects, certainly at least three trial projects.

Nick Grasberger - *Harsco Corporation - President & CEO*

Yes.

Bryan Carlson - *Atlantic Investment - Analyst*

(Multiple speakers) sites. I know that -- I believe that you were able to renegotiate two and you exited one.

Nick Grasberger - *Harsco Corporation - President & CEO*

Right.

Bryan Carlson - *Atlantic Investment - Analyst*

Would you be surprised to see that kind of success going forward? Or would you believe that it should be better success with the larger number of contracts? Or you ought to be more aggressive to more quickly remediate the situation one way or the other?

Nick Grasberger - *Harsco Corporation - President & CEO*

I have to say, every situation is different. It's very difficult to kind of predict what the outcome will be. But recognizing that even in those cases where we choose to stay, there are things that may have to happen in the future to make them acceptable performers, right? Again, the analysis is stay or exit. And in some cases, given the exit costs, even with a relatively modest improvement in the contract, you're better off staying than exiting.

Bryan Carlson - *Atlantic Investment - Analyst*

Okay. And I think that your outlook around 2015 in fact doesn't sound like it's changed that much. But I think because of Q4 makes 2014 a fair bit lower, and you've tried to give confidence around 2015, but that the way it's been phrased, I think, the way it's been communicated, people want to just say way, well it's 12%.

And I think that that's probably the reason the stock is down over 10% today. So to the extent that you can clarify, or help people to understand sort of the assumptions that you have had, and apparently continue to have around 2015 improvement, I think that would be helpful.

Nick Grasberger - *Harsco Corporation - President & CEO*

Well, our assumptions are around 2015 have not changed in a material way. And as we indicated, our definition of moderate is certainly beyond 12%.

Bryan Carlson - *Atlantic Investment - Analyst*

Thank you.

Operator

You have a follow-up question from the line of Glenn Wortman with Sidoti and Company.

Glenn Wortman - *Sidoti & Company - Analyst*

Thanks, guys, for taking another question here. Let me make sure I understood what the previous caller was saying, or I heard him right about the projected operating income benefit from improved contract mix within Metals & Minerals, say, over the next several years. Have you guys put a number on that?

Nick Grasberger - *Harsco Corporation - President & CEO*

When we launched Orion, we kind of broke down the components of the improvement in the business over the next three years. One component was the cost reduction, the so-called simplification exercise. And then we had another sizeable component of improving performance on the base contracts, either to exit or through renegotiation, or some contracts ramping up. So that was over half of the benefit that we expected over the next three years to deliver the targets that we laid out.

Glenn Wortman - *Sidoti & Company - Analyst*

Okay. Thank you.

Operator

You have a question from the line of Will Nasgovitz with Heartland Advisors.

Will Nasgpovitz - *Heartland Advisors - Analyst*

Congratulations on the free cash flow generation in the quarter. Did you lay out potential CapEx guidance for next year?

David Martin - *Harsco Corporation - Director of IR*

We talked about that before. We've -- because we've indicated that 2014 was really the high watermark in terms of capital spending. And even though it's going to be a bit lower than we thought earlier in the year, 2015 will be yet lower. So we would expect 2015 capital spending to be in the $160 million, $170 million range, something like that.

Will Nasgpovitz - *Heartland Advisors - Analyst*

Thanks very much.

David Martin - *Harsco Corporation - Director of IR*

Yes.

Nick Grasberger - *Harsco Corporation - President & CEO*

Thank you.

Operator

And there are no other questions at this time.

David Martin - *Harsco Corporation - Director of IR*

Okay. Thank you Carmen, and those that listened to and participated in our call today. We do appreciate your interest in Harsco. A replay of this call will be available later today through the 6 of December. And the replay details are included in our press release this morning.

If anyone does have any follow-up questions, please do contact me, as my e-mail and phone number details are included at the top of the earnings release from this morning. And lastly, we do look forward to speaking with you in the future. And have a good day.

Operator

Thank you again for participating in today's teleconference. You may now disconnect.
