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PRESENTATION

Operator

Good morning. My name is Joey and I'll be your conference facilitator. 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 now introduce Mr. Dave Martin. Mr. Martin, you may begin your call.

Dave Martin - *Harsco Corporation - Director of IR*

Thank you, Joey. And welcome to everyone joining us. I'm Dave Martin, Director of Investor Relations for Harsco. With me today is Nick Grasberger, our President and Chief Executive Officer; and also Pete Minan, our Senior Vice President and Chief Financial Officer. This morning we will discuss our results for the third quarter of 2015 and our outlook, and update you on our strategic priorities and then we'll take your questions.

Before our presentation, however, let me take care of a few administrative items. First, we did issue two news releases this morning. The first was an announcement stating that we are pursuing options for the separation of our Metals and Minerals segment from our other businesses, and subsequently we issued our Earnings Release for the third quarter. A PDF of these releases as well as the slide presentation for this call have been posted to the IR section of our website.

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 those 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 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 Earnings Release issued today as well as the slide presentation.

Now I'll turn the call over to Nick Grasberger to begin our prepared remarks.

Nick Grasberger - *Harsco Corporation - President and CEO*

Thank you, Dave. Good morning, everyone. Thanks for joining our call. Let me start with the announcement concerning the separation of our Metals and Minerals business.

Our strategy over the past two years following the formation of the Brand joint venture has been to fix the Metals and Minerals business, grow the Rail and Industrial businesses, and develop a lean, active corporate team, all with a focus on improving return on capital and enhancing shareholder value. Put simply, we are very pleased with the progress we have made against those objectives. While it has been difficult to overcome the precipitous cyclical declines in the steel, energy and commodity sectors, we believe Harsco is much better positioned today to grow and deliver above-market returns as these sectors recover.

It has also become clear to us that the separation of Metals and Minerals from the Rail and Industrial businesses is the next logical step to unlocking shareholder value and optimizing the returns of the individual businesses. Our efforts in Metals and Minerals to improve core processes, address underperforming contracts, remove excess cost and build a more effective organizational structure have enabled us to now follow this path. So now we have reached an important milestone and believe the separated businesses would provide more targeted and compelling value propositions for their respective stakeholders.

The form of the separation will of course take some time to finalize as we explore all options. The Harsco management team and our Board of Directors, supported by Goldman Sachs and other advisors, will pursue the best outcome for all stakeholders. In the meantime, we will continue to navigate the course we have chartered and drive towards the financial goals we have set for each of our businesses.

Turning to our third-quarter results, our key financial metrics were above expectations due to better product mix in Rail and lower costs across each business and at corporate. And although market conditions are weaker than anticipated in steel, commodities and energy, our earnings guidance is little changed for the full year. You'll note we highlighted a few special items in the quarter related primarily to an M&M site closure in the UK, and the resolution of a few longstanding items around environmental and litigation matters in M&M. Pete will cover these in more detail in a few minutes.

As we look ahead to 2016, we expect continued core growth in Rail excluding the FX gain in 2015, but difficult markets to persist in steel, energy and commodities. Although significant cost has been removed in M&M, Industrial and at corporate, further actions are under way.

I have commented before that our deep dive into M&M's operations through Project Orion has uncovered additional opportunities to streamline our cost structure, both in our customer sites and in the support functions. Therefore, we are targeting an additional $20 million to $25 million of cost reductions beyond the $35 million to $40 million already realized. These incremental savings, coupled with the year-over-year benefits of the triage efforts related to the under-performing contracts, should mitigate the ongoing volume pressure at our customer sites.

Before I turn the call over to Pete I would like to comment on the change in our dividend. It was a very difficult decision for the Board but we believe the responsible action to take given the economic conditions and weakness in many of our end markets. Harsco is proud of its longstanding practice of returning capital to our investors and remains committed to a healthy balance between a strong capital structure and shareholder returns.

I'll now turn the call over to Pete.

Pete Minan - *Harsco Corporation - SVP and CFO*

Thanks, Nick. And I'm on slide 5. Adjusted operating income in Q3 of $35 million was above our guidance range of $20 million to $25 million as performance in our Rail and Metals segments were better than anticipated, and also corporate spending was lower than we had forecasted. In Rail, we benefited from the acceleration of area spare parts and service revenues. In Metals and in corporate, results were aided by our efforts to control overhead costs.

Compared to 2014 quarter, operating income declined, with each business unit reporting lower earnings compared with the prior-year quarter, as we expected. Revenues in the quarter also declined as expected to $428 million, and this represented a decrease of 19% year over year. The impact of the strong US dollar was the primary driver of this change, as was the case in preceding quarters. Additionally, revenues were impacted by lower steel production, reduced commodity prices and site exits in Metals, along with lower Industrial products demand and a less favorable mix in Rail.

Earnings per share was $0.18 in Q3 as compared to our guidance range of $0.05 to $0.09 as a result of the higher adjusted operating income. Compared with the prior-year quarter EPS declined $0.13 and in the just completed quarter included equity income of our Brand Energy joint venture of approximately $3 million. This figure translates to an EPS impact of roughly $0.02 after-tax and compares to equity income of $5 million in the prior-year quarter.

Free cash flow for Harsco for the quarter was $23 million, which was better than we forecasted internally primarily due to higher cash earnings and the underspending of capital. Meanwhile, free cash flow declined $42 million versus the third quarter of 2014 as fewer contract advances offset reduced capital spending.

Also as detailed in our Earnings Release, we recorded a number of unusual items in the quarter. As in the past, a number of these items are connected to Project Orion as we continue to review our sites including those that are underperforming to identify opportunities to improve returns and possibly exit sites where we see that as the best outcome.

Additionally, there were few other adjustments in the quarter. One is related to a site where we have curtailed a portion of our operations after a European customer decided to close its liquid steelmaking operation. As you know, customer site closures have occurred only on a very limited basis to us in the past but this is a consequence of and, in fact, illustrates the current challenges within the steel industry.

With this now behind us, we are generally comfortable with the sustainability of our customer portfolio and are hopeful that similar situations will not develop in the future. We spend considerable time assessing where best to be positioned strategically within the industry but, as you know, steel fundamentals will dictate how much additional right-sizing or restructuring may be required at our customer sites.

In total, the unusual items totaled to $27 million or $0.28 per share for the quarter. These include $14 million for receivables, asset impairments and severance accruals related to the European steel customer that curtailed operations, $11 million of site exit costs and contract resolution charges related to a few underperforming sites, $2 million for external costs incurred to date for the planned separation of Metals and Minerals, and a $1 million tax trueup adjustment tied to the 2013 Infrastructure transaction.

Looking forward, we will likely incur additional costs through the M&M strategic review process and as we implement additional cost reduction activities. Also it is possible that we will incur additional costs as we continue to evaluate our underperforming sites, but otherwise we continue to believe that these types of charges are largely behind us.

Let me change to slide 6. In the third quarter, Metals and Minerals generated operating income of $21 million, which was better than we had expected, due primarily to lower overhead costs. The result compares to operating income of $27 million in the prior-year quarter.

During the quarter lower costs attributable to Project Orion and other factors were offset by lower commodity prices in demand, reduced customer LST, site exits and foreign exchange impacts. Customer LSTs in the quarter declined 10% year over year in absolute terms, and this change reflects the fact that we exited sites in the past year, and it also accounts for lower customer production in our three largest operating regions, Europe, North and Latin America.

On a same-store sales basis, our LSTs decreased approximately 5%, which mirrors the broader steel industry trend in the quarter. Free cash flow year to date in Metals totaled $47 million as compared to $6 million in the prior year, with this improvement attributable to both lower capital spending and working capital. The increase in free cash flow within Metals is certainly noteworthy given the pressures on cash earnings. Now there's much more work to do here and we continue to focus on pulling cash from working capital and lowering our investments as needed.

Turning to slide 7, our Industrial business generated operating income of $14 million in the third quarter as compared to $16 million in the third quarter of 2014. This change resulted from lower demand for our heat exchanger and commercial boilers products which was partially offset by lower overhead costs. As a result, operating margins were relatively stable at 15%.

Free cash flow year-to-date totaled $40 million versus $41 million in 2014 as capital expenditure related to our CenterPoint investment in Tulsa and lower cash earnings has been offset by improvements in working capital. And, lastly, our backlogs declined just over 20% sequentially, as can be expected, and our current backlogs continue to represent approximately three months of segment revenues.

We continue to make efficiencies improvements in anticipation of continued weakness in Industrial but there are rays of light in this business. Order rates for our Industrial grating business remain steady. Order rates for commercial boilers have improved modestly in recent months, and quarter-end backlogs for these products are now above prior-year levels. And although backlogs for heat exchangers have contracted, new bookings for coolers have stabilized over the past quarter, albeit from a low base.

Now Rail on slide 8, operating income in Rail was $8 million and better than anticipated in the quarter due to mix and timing of some spare parts and service revenues. The result compares to operating income of $15 million in the prior year period, with the year-over-year change attributable to fewer equipment and spare parts sales, as we had expected.

Meanwhile our free cash flow in Rail has declined year to date due to fewer customer advances on large contracts. This change is more reflective of the lumpiness of these cash advances as opposed to any indicator of longer-term trends in the business. Also, our backlogs at the end of this quarter totaled nearly $340 million.

As we've discussed in the past, we expect to realize some revenue during the fourth quarter under our contracts with SBB. These impacts will accelerate in future quarters. And while we were not awarded any large tenders in the quarter that are noteworthy, the growth opportunities within the maintenance of way market remains significant and we remain confident in our ability to win and execute against these potential contracts.

Slide 9 -- regarding our 2015 outlook, we tightened the ranges for adjusted operating income and adjusted earnings per share. Adjusted operating income is now expected to be between $125 million and $130 million, and adjusted EPS between $0.46 and $0.50 per share.

In Rail, the timing benefits in Q3 will reverse in the fourth quarter. And our expectations for Industrial have not changed. And in Metals we've taken measures to further control costs since seeing our Q3 results, and we're beginning to see some maintenance and operational improvements at some of our more challenging locations, including those in South America. However, these benefits will be offset by lower steel production and commodity prices for the balance of the year as well as steel mill closures.

Our capital budget for 2015 is now roughly $120 million as compared with $140 million previously as a result of reduced spending within Metals. Our free cash flow forecast for the year is now $50 million to $60 million.

Let's move to slide 10. Regarding our fourth quarter, we expect operating income to be between $15 million and $20 million as compared to $29 million in the fourth quarter of 2014. For Metals and Minerals, as you know, the fourth quarter is historically comparatively weaker than the earlier quarters of the year as a result of holiday slowdowns in many of our customer sites.

As compared to the prior year, operating income is expected to decline owing to LST, site exits, customer shutdowns and lower nickel and scrap demand. These declines are offset partially by cost reductions initiatives in Q4. And as Nick mentioned and as I will mention later, we have begun other cost reduction initiatives which will have a significant impact in 2016.

For Industrial, operating income is expected to decrease with reduced demand partially offset by lower SG&A costs. And in Rail, earnings are anticipated to increase due to higher equipment and spare parts sales. And corporate costs will be lower year over year. Lastly, on Brand, we are expecting to record equity income of approximately $1 million in the fourth quarter, which reflects additional non-cash foreign exchange and energy market impacts in the next quarter as compared to our prior outlook.

And before I turn to Project Orion let me comment on our financial position. Net debt declined $75 million in the quarter. And we ended the quarter with net debt of $801 million, a leverage ratio of 2.7 times, and gross liquidity of approximately $450 million.

Now, as you know, we decided to repay our $250 million of notes due in October with funds provided from a revolving credit agreement. This provided an attractive cost of financing and continues to provide ample liquidity to manage our businesses.

In recent months we've been exploring long-term refinancing options for this debt. This process is continuing and we believe we are in good position now to advance this process over the next few months. At this point we can't comment much further on these efforts, although again I would highlight that we remain comfortable with our financial position and flexibility.

Now turning together Project Orion on slide 11, we remain pleased with the progress against all major initiatives under Project Orion, and the initial work contemplated under the project to improve business returns are nearing completion. We realized approximately $6 million of workforce related savings in Q3, and the ongoing benefits from these workforce and operational improvements now exceeds $36 million.

Regarding our underperforming contracts, or UPCs, we finalized solutions at 65% of the original UPCs as of the end of the quarter. This means six were finalized since our last call in August. Of those recently finalized, four are targeted for exit and these include two sites which are among our lowest performing sites, and we are pleased with these outcomes.

And, as in the past, it's important to highlight that the financial performance at our finalized sites continues to improve despite external headwinds. Margins at these finalized sites are now comparable to our performing sites and further benefits are expected in the future as UPC solutions reach a full run rate. Of the remaining 24 underperforming sites, 13 are in progress and we continue to anticipate that we will address the remaining underperforming sites by early 2016.

And, lastly, let me comment on the other improvement initiatives under way within M&M. As discussed in August, we are focused on levers that will reduce both cost of sales and SG&A. Key areas for improvements expected include labor productivity, equipment utilization and maintenance, and cost of consumables such as fuel and tires.

Each region and site has been tasked with initiatives to realize certain operating and related cost improvements, and we expect benefits from these efforts to materialize over the next year. Savings are targeted to be $20 million to $25 million. And we expect that the majority of this benefit will be realized in 2016.

That concludes our prepared remarks and at this point we would be happy to take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

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

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

Can you just talk about the tax dynamics or tax basis on the Metals and Minerals business, and how you're thinking about timing for when you make a decision on sale or spin or what to do?

Pete Minan - *Harsco Corporation - SVP and CFO*

Jeff, it's Pete. As Nick mentioned, we're just pursuing options now and all options are being considered. So, we haven't reached resolution as to which route we take, whether it's a sale or a tax-free spinoff. Naturally the tax basis and potential for tax leakage will inform that decision but we're going to ultimately conclude on that in the early part of 2016 and reach a conclusion for whatever we think generates the best value for the shareholders.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

Okay. And then how does this impact how you're thinking about your balance sheet refinance? And I know you moved it into the revolver but how are you thinking about capital structures going forward and how you want to have the balance sheet set up from a refinancing standpoint?

Pete Minan - *Harsco Corporation - SVP and CFO*

Jeff, for the past several months we've been, as you know, pursuing options to refinance the bonds that were due in October and we considered market conditions and try to balance that with our need for flexibility financially and appropriate pricing. Obviously in the meantime we put the bonds on the revolver.

Notwithstanding that, we're still continuing our plans to refinance that debt on a longer-term basis. So, really there's no change in that direction at all. We continue to pursue it and we hope to have clarity on that in the next couple of months.

As far as the capital structure to the remaining businesses, that's all something that will be considered as we get closer to evaluating the options that we're facing with respect to separation of the business.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

Okay. And then just a housekeeping item -- can you quantify FX headwind and exited contracts headwind on a revenue basis in M&M this quarter?

Pete Minan - *Harsco Corporation - SVP and CFO*

Let me start with the latter. The impact of loss contracts from a revenue perspective on the quarter, year-on-year comparison, was a decrease of $17 million. And the impact of the same on operating income was about $4 million.

As far as the FX headwinds, about $2 million quarter on quarter and it's continuing at the same rate as it was before for the full year, $10 million to $15 million. That's all operating income. I'm sorry, Jeff, you asked about revenue and its impact on operating. Do you have the number on revenue, Dave? I don't have that handy.

Dave Martin - *Harsco Corporation - Director of IR*

It would be right around $200 million.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

On a full year basis?

Pete Minan - *Harsco Corporation - SVP and CFO*

Yes.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

And do you have it in the quarter?

Dave Martin - *Harsco Corporation - Director of IR*

It was $47 million.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

Okay. Thanks, guys, I'll get back in queue.

Operator

(Operator Instructions)

Your next question comes from the line of Bhupender Bohra from Jefferies.

Bhupender Bohra - *Jefferies & Co. - Analyst*

Hi, good morning, guys. I just wanted to talk about Brand Energy here. You guys took down the guidance. Could you talk about that and give some color on it?

Nick Grasberger - *Harsco Corporation - President and CEO*

Yes, it's Nick. When the joint venture was formed back in 2013 on a pro forma basis we were looking at EBITDA in the $310 million, $320 million range, something like that. And it improved based on synergies and some market lift in 2014 up to, say, $360 million, $365 million. The decline back to the 2013 pro forma level is mostly around FX and market conditions. Clearly, there had been other charges and costs related to integrating the businesses but it's really mostly around FX and energy.

Now, you'll recall that the Brand business is more exposed downstream, and so the impact of energy CapEx has been somewhat muted in Brand relative to other energy-driven businesses. And, also, much of the work they do is associated with long-term contracts, which also tends to dampen any volatility.

So, that's effectively why the business is where it is. In terms of equity income, we continue to be affected by currency as well on some inter-Company loans that they have that are below the operating income line but affect our equity income.

Bhupender Bohra - *Jefferies & Co. - Analyst*

And how should we think about this going forward, do you have some color on (inaudible)?

Dave Martin - *Harsco Corporation - Director of IR*

Sorry, Joey, we have a lot of noise in the room, so, Bhupender, if you could repeat that question that would be helpful?

Bhupender Bohra - *Jefferies & Co. - Analyst*

Just wanted to get some color on 2016, how should we think about Brand joint venture going into 2016?

Nick Grasberger - *Harsco Corporation - President and CEO*

I think that it's difficult to say at this point. Clearly we would expect or hope that the FX headwinds would mitigate to some degree and have an easier comp year over year, both on operating income as well as on the inter-Company loans. As you know, the energy markets really began to take a downturn early in 2015 so we'll have a difficult comp at least through the first quarter.

What I will say, though, is that the integration of the businesses is complete. I think the management team there is doing an excellent job. They've taken out a lot of cost, both through the integration and since the integration. And we remain very confident in their ability to execute and ultimately in the value that we will realize when our stake is monetized.

Bhupender Bohra - *Jefferies & Co. - Analyst*

Okay, just one more question here. Now the thinking is you want to spin off or do some transaction on M&M business. At the same time, you talk about how you want to grow your Industrial and Rail business if you can. Just give us some color on your M&A funnel here in those two businesses.

Nick Grasberger - *Harsco Corporation - President and CEO*

First of all, the plan certainly is to grow M&M and Industrial and Rail, despite what we experienced in M&M as we've exited contracts and currency and economic conditions have hurt the business. We do believe that M&M is well positioned to grow, as well. But largely organically, I'll say.

In terms of Industrial and Rail, we do have a fairly sizeable pipeline of M&A. We've done three although somewhat smallish transactions over the past year or so, two in Rail and one in Industrial. And I would anticipate that we'll do more of the same. But I think it's unlikely that you'll see a very sizeable deal in either one of those sectors in the near term.

Bhupender Bohra - *Jefferies & Co. - Analyst*

Okay. Dave, just a question on the LST. What are your expectations for the year now?

Dave Martin - *Harsco Corporation - Director of IR*

Yes, we have reduced our LST forecast for the full year. The assumption is that LSTs will contract about 7% 2015 versus 2014.

Bhupender Bohra - *Jefferies & Co. - Analyst*

Thank you, guys.

Operator

Your next question comes from the line of Jeff Hammond.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

Hi, guys, just a couple follow-ups here. One, just thinking about 2016, can you talk about some of the additional headwinds that might offset some of these savings in M&M into 2016? And it sounds like you're going to get $20 million to $25 million. Most of that would be in 2016 but can you quantify maybe total savings in 2016 for M&M?

Pete Minan - *Harsco Corporation - SVP and CFO*

It's still a little early, Jeff, to provide a whole lot of detail on 2016. But we are expecting that the headwinds and market pressures that we're experiencing presently will continue. So, LST decline, certainly commodity, nickel and scrap prices will continue to be where they are. So, those will be pretty significant headwinds. However, we expect those headwinds to be essentially mitigated by those very cost actions you're referring to.

So, while we haven't quantified precisely how much of the $20 million to $25 million will be in 2016 it is substantially or most of it. We're still in the process of narrowing that down. But long story short, M&M results should be consistent with 2015 as the improvement initiatives get realized in 2016.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

Okay. And then for Rail, you have the Swiss contract coming on. Is it simple enough to think about the delta of 2015 to 2016, as that Swiss contract coming in?

Pete Minan - *Harsco Corporation - SVP and CFO*

Yes. If you look at Rail performance, excluding the impact of that foreign exchange gain we had in Q1, you should definitely see some improvement there as a result of the full acceleration of the SBB deliveries in 2016.

Jeff Hammond - *KeyBanc Capital Markets - Analyst*

Okay, thanks guys.

Operator

(Operator Instructions)

There are no further questions at this time. I'll turn the call back over to the presenters.

Dave Martin - *Harsco Corporation - Director of IR*

Yes, thank you, Joey, and to those that listened to and participated on this call this morning. A replay of this call will be available later today through November 23 and the replay details are included in our Earnings Release from this morning.

Lastly, if you have any follow-up questions, please contact me, and my contact details are included at the top of today's Earnings Release. Thanks again. We look forward to speaking with you in the future. And have a good day.

Operator

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