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LECO - Q1 2014 Lincoln Electric Holdings Inc Earnings Conference Call

EVENT DATE/TIME: APRIL 23, 2014 / 1:00PM GMT

OVERVIEW:

Co. reported 1Q14 consolidated sales of \$685m and EPS of \$0.69.



CORPORATE PARTICIPANTS

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PRESENTATION

Operator

Greetings and welcome to the Lincoln Electric 2014 first quarter financial results conference call. At this time, all participants are in a listen-only mode. As a reminder, this call is being recorded. It is now my pleasure to introduce your host, Vincent Petrella, Executive Vice President and Chief Financial Officer. Thank you, sir. You may begin.

Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

Thank you, Danielle, and good morning. Welcome to the Lincoln Electric 2014 first quarter conference call. We released our financial results for the quarter this morning, prior to the market's open, and our release is available on the Lincoln Electric website at LincolnElectric.com, or by contacting our investor relations office at 216-383-2534.

Joining me on the call today is Chris Mapes, Lincoln's Chairman, President, and Chief Executive Officer. Chris will begin the discussion this morning with an overview of the quarter and then I will cover the numbers in more detail. Following our prepared remarks, we will take your questions.

As part of our webcast today, we are using a slide presentation, which can be accessed on our website under the Company and investor relations tabs. But before we start our discussion, please be reminded that certain statements made during this call and in our discussions may be forward-looking and actual results may differ from our expectations. Actual results may differ materially from such statements due to a variety of factors that could adversely affect the Company's operating results. Risks and uncertainties that may affect our results are provided in our press release and in our SEC filings on Forms 10-K and 10-Q.

Additionally, we discuss financial measures that do not conform to US GAAP, and you may find important information on our use of these measures and the reconciliation to US GAAP in the financial tables that we have included in our earnings release. With that, let me turn over the call to Chris Mapes. Chris?



Chris Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO, President*

Thank you, Vince, and good morning to everyone joining us on the call today.

Moving to slide 3, our first quarter profit and earnings performance showed good resilience despite a slow start to the year, which impacted topline performance. In the quarter, sales declined 4.7% to \$685 million, driven by 5% lower volumes, which offset the benefits we achieved from acquisitions and steady price performance.

Volumes declined across most reportable segments on ongoing choppy and uneven demand. However, we did realize generally steady demand for consumables as well as growth in automation. The most notable volume weakness was in our North American equipment business and primarily in exports, which we attribute to lower international industrial demand. In North America, equipment remains soft on a slow start to the year, and due to challenging year-over-year comparisons, as Q1 2013 equipment sales were a record for the organization.

While we were disappointed that the volume growth momentum achieved in the fourth quarter was not sustained, operational initiatives, favorable mix, and careful management of expenses protected margin performance. At the gross profit line, margins increased 150 basis points to 33%.

Looking at operating profit on an adjusted basis, operating profit margins remained resilient, increasing 50 basis points to 14.3% in the quarter. While our Venezuelan results contributed to both gross profit and operating margin performance, we are pleased to report that we would have still showed steady to slightly higher year-over-year margin performance if we had completely excluded Venezuela.

Now on a reported basis, our operating profit margin declined 60 basis points to 11.6%. This decline is primarily due to an \$18 million charge reflecting the re-measurement loss of our Venezuelan Bolivar-denominated monetary assets. Vince will speak to this in more detail in his section.

On a reported basis, EPS declined 14% to \$0.69, again due to the impact of the Venezuelan charge. Adjusted EPS held reasonably steady at \$0.91 for the quarter, down \$0.01 compared with the prior year.

Cash flow was positive and the return of cash to shareholders remained strong at \$70 million through share repurchases and dividends. These actions reflect our continued confidence in the business and our ability to execute on our long-term strategy and deliver on our 2020 goals.

Moving on to slide 4. Customer demand trends have been challenging. While we did see volume trending improving through the first quarter with March sales, our order rates and backlogs notably stronger, we still did not achieve positive sales growth on a year-over-year basis in March, and now in April.

And, while we were capitalizing on strong and improving end sectors such as energy, automotive, rail, maintenance and repair, and to some degree construction, general sluggishness in regional economies and in industrials has offset any notable gains. As such, we remain cautious and continue to monitor customer and channel trends closely, and anticipate only a very modest uptick in demand in the second half of the year.

Moving on to slide 5, we continued to stay focused on delivering on our strategic goals, capitalizing on opportunities, and addressing the near-term market risks. While we have aligned our expenses and cost control measures with the current demand environment to further protect margin performance and cash flow, we are continuing to invest in the business where prudent to drive topline and margin growth long-term.

A few key areas to highlight are: our automation integration efforts continue, which align our recent automation acquisitions from late 2012 and 2013 into an expansive automation solutions portfolio. We are also focused on the continued ramp up of our greenfield automation business in Brazil.

Our nickel alloy expansion, I am pleased to report that we are in the final stages of integrating our Techalloy manufacturing platform into our Northeast Ohio footprint. We expect this move will result in higher product quality, shorter cycle times, and lower working capital requirements for the business.

Our Asia Pacific segment performance continues to be challenged from local market dynamics. Additionally, we are reorienting our strategy in China to focus on higher value-added solutions and customers seeking welding solutions and application expertise, which we expect will yield modest improvement in sales and margins in late 2014.

In North America, we continue to drive sales force efficiency with new CRM tools, hardware, and enhanced training. We expect these efforts will not only provide greatest greater service levels to our customers, but also to increase sales capacity to drive growth.

Lincoln Electric has a strong track record of operational efficiency, driven by the hundreds of lean programs initiated across our global platform each year. In addition to these programs, we are proud to be investing in a new printed circuit board platform in northeast Ohio, which will act as a global center of excellence for our inverter-based equipment offering. This effort has been underway for several months and we expect to launch our new facility in the third quarter.

We anticipate numerous benefits from this investment, which include enhanced quality, reduced cycle times, and an ability to protect and expand our technology globally. Additionally, we are leveraging our investment in SAP, which is starting to provide greater visibility through its data and management tools, with seven additional SAP rollouts slated for 2014. We are pleased with our investment and continue to anticipate benefits over the long term.

So as I pass the call to Vince to cover the quarter in more detail, I would like to reemphasize that, while volumes are soft due to a slow start of the year, we are seeing steady performance in consumables, growth in automation, and our margin, earnings, and cash flow performance remains resilient while we are continuing to invest in our business.

And, now, I will pass the call to Vince.

Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

Thank you, Chris. Now, walking through the income statement highlights on slide number 6, our consolidated sales were down 4.7% compared with the first quarter of 2013. Volumes decreased reported sales by 5% and pricing was up 40 basis points. Foreign-exchange had a negative 1.2% impact on sales, and acquisitions contributed an increase of 1.1%.

First quarter gross profit margins increased to 150 basis points to 33% compared with 31.5% in the comparable prior year period. We had LIFO charges in the quarter that totaled \$1 million and the prior year's first quarter had LIFO charges of \$1.6 million.

The improved gross margins were primarily driven by a better sales mix, operational improvements, and higher margin contributions from Venezuela. The SG&A line includes a \$17.7 million charge related to the re-measurement of the Venezuela operations financial statements at quarter end. Prior-year SG&A included an \$8.1 million charge from a devaluation of the Venezuelan currency.

Excluding the Venezuelan foreign exchange losses in both years, SG&A expenses were flat in 2014 compared to 2013. Excluding these charges, SG&A would have been 18.7% of sales, an 80 basis point increase over the prior year.

Operating income for the quarter declined 60 basis points. The prior year's quarter included rationalization charges of \$1.1 million, primarily related to actions and asset impairments in North America and Asia-Pacific. Adjusted operating income before rationalization charges and charges related to the Venezuelan foreign-exchange losses was \$98.1 million, or 14.3% of sales, a 50-basis-point improvement over the prior year.

The effective tax rate for the first quarter was 31.5% compared with 26.3% in the prior year's first quarter. The prior year's first quarter tax provision included discrete items related to the reinstatement of the US R&D tax credit and decreases in valuation allowances. Other factors driving this lower effective tax rate in 2013 were earnings in lower tax rate jurisdictions and utilization of foreign tax credit carryforwards.

Diluted earnings per share decreased 13.8% for the first quarter compared with the prior year. Excluding the previously referenced special items, adjusted diluted earnings per share decreased \$0.01 per share in 2014 compared with 2013.

The higher year-over-year effective tax rate reduced EPS by approximately \$0.05 per share, and share repurchases increased EPS by about \$0.03 per share.

On a reportable statement basis and excluding special items, North America Welding adjusted EBIT margins declined by 70 basis points in the first quarter on lower volumes. Lower equipment sales were related to our export and international markets, while domestic demand trends held relatively steady. Year-over-year volume performance improved in March, compared with January and February.

Europe Welding's adjusted EBIT margin declined 90 basis points in the quarter. The decline was attributable to a 5% reduction in year-over-year volumes and a 1.4% decline in pricing. We did experience better topline results in the UK and in parts of Eastern Europe, while we had weaker sales in the Netherlands, Russia, and in France.

The Asia-Pacific segment recorded an adjusted EBIT loss in 2014. Our sales in Asia-Pacific were down 7.7% due to volume, and pricing declined 50 basis points. The volume decreases were primarily caused by the continuing softness in industrial markets in China. And, in addition, Australian volumes declined as a result of lower mining activity, as well as general industrial sluggishness.

South America Welding adjusted EBIT margin increased to 26.7% compared with 14% in 2013 because of significant improvements in our Venezuelan operations and strong pricing actions. The price increases were primarily caused by the higher inflationary environment, particularly in Venezuela.

The South American segment also included a \$17.7 million charge related to foreign exchange losses and \$9.7 million in charges in 2013 related to the Venezuelan currency re-measurement and devaluation in the prior year.

On March 31, 2014, we moved our Venezuelan exchange rate from 6.3 bolivars to the dollar to the SICAD I rate of 10.7 bolivars. In addition to the \$17.7 million foreign-currency loss recorded in the first quarter, we expect additional charges of \$3.5 million in the second quarter as we liquidate inventory valued at historical exchange rates.

We also expect the use of the higher SICAD I rate to result in lower reported earnings from our Venezuelan operations in the future. The continuing uncertainty surrounding operational activity and currency exchange transactions will likely result in further volatility from our Venezuelan business.

The Harris Products Group first quarter EBIT margins declined by 40 basis points. Declining precious metal prices resulted in less margin contribution. Volumes increased slightly on improvements in retail programs and consumables demand.

During the quarter, we paid a dividend of \$18.6 million compared with no cash dividend in the prior year's first quarter. We paid the prior year's first quarter dividend in the fourth quarter of 2012 as an additional dividend payment amounting to \$16.5 million. This dividend would normally have been paid in January of 2013.

Our first quarter capital spending was relatively consistent with the prior year at \$14.5 million. Our 2014 capital spending plan is currently estimated to range from \$60 million to \$80 million, primarily focused on significant reinvestment projects in our North and South American businesses.

During the quarter, we spent \$51 million repurchasing about 710,000 shares and the quarter also included \$20 million of voluntary contributions to our US pension plan. We ended the quarter with no net debt and over \$205 million of cash on our balance sheet. We will continue to invest in the business for the long run and more aggressively return our cash to shareholders.

With that, I would like to open the call for questions. Danielle?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Schon Williams, BB&T Capital Markets.

Schon Williams - BB&T Capital Markets - Analyst

The topic of the day, South America, maybe we will start there. As we enter the year, it sounds like you guys -- you stopped sending product from North America into that region.

I am just wondering, was some of -- were you still working off inventories during Q1 from North America that may have helped the margins? I am trying to get a sense of when exactly should we start to see some of that margin compression. Is it happening as we enter Q2? Is it more of a second half of the year? I am just trying to get a sense of how the timing plays out through the year for the margin profiles in South America.

Chris Mapes - Lincoln Electric Holdings, Inc. - Chairman, CEO, President

Sean, I would tell you there is a confluence of factors that will drive our Venezuelan operations to lower margins in the future, including the second quarter. We will be translating those financial statements at 10.7 bolivars versus 6.3 bolivars, so that the translated bolivars and the US dollars will be considerably less affecting our earnings stream.

We are sourcing raw materials at a higher cost to limit our hard currency US dollar exposure to the country. There will be the \$3.5 million of charges rolling through COGS related to the inventory that is on-site.

And, lastly, the item that you mentioned, we are selling down the inventory of traded products there that have come into the country from the US, and that will also have an impact on our business in the future.

Schon Williams - BB&T Capital Markets - Analyst

Okay. And then, maybe just turning to the Harris division, I know that raw materials have been a bit of a headwind it there. It looks like it is going to continue at least into Q2.

Do you feel like -- I mean, it certainly led to some margin compression this quarter versus last year. Should we continue to see that -- I mean, until we start to see some of the raw materials bounce back up, do you think that margin compression is going to be kind of the norm over the next quarter or two?

Vincent Petrella - Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer

I think we have got an unfavorable comp versus the metal side, probably, that remains with the business in Q2. I will tell you I was happy to see that we actually had gross margin expansion within that business on a year-over-year basis.

So I actually think that we get the Q2 comp behind us, primarily relative to the cost associated with silver and the [adders] that are involved in that commercial transaction, and then we will start to have a clearer comparison on silver costs as we go through the back half of the year. But, again, our gross margin expansion year-over-year for the Harris business in Q1.

Operator

Mark Douglass, Longbow Research.

Mark Douglass - *Longbow Research - Analyst*

Vince, looking at the Venezuela of course, going forward and yet really strong pricing in the quarter, are you going to be able to keep that up? I think they had some cost controls and gross margin controls in the country and things like that. Is that also going to significantly impact your ability to generate the earnings in Venezuela?

Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

Well, we are going to continue to run the business in the same fashion, Mark, that we have historically in terms of pricing. There is a highly inflationary economy there, and as costs go up, we will endeavor to raise our top line. So we are very familiar with the margin control legislation that was passed recently in country, but we will continue to operate our business as we have heretofore and attempt to cover the highly inflationary increases with pricing increases.

Mark Douglass - *Longbow Research - Analyst*

Okay. And just to confirm, 1Q was still translated at the 6.3 bolivars?

Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

That is correct, Mark. We translated the whole of the first quarter at the official rate of 6.3 bolivars and on March 31, 2014, we translated the balance sheet at the new 10.7 bolivars rate. So as we move forward, the P&L and the balance sheet will be translated at whatever the SICAD I rate might be in the next month and quarter. And that could move around a little bit because it is an auction-based rate, but the 6.3 bolivars rate, correct, translated the income statement in the first quarter.

Mark Douglass - *Longbow Research - Analyst*

Okay. So then have you been able to actually get dollars at SICAD I? What would be the risk of going to SICAD II?

Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

Well, we have been able to get very few dollars using any foreign-currency exchange mechanism compared with historical activities. There was always a risk of a higher rate being used by Lincoln in the future. But, at the present time, we believe the most appropriate rate to translate our financial statements and our net monetary asset position is the SICAD I rate.

Operator

Kathryn Thompson, Thompson Research Group.

Kathryn Thompson - *Thompson Research Group - Analyst*

If we could just step back and just look broadly, more -- demand for the year and really going even to the following year. But in light of first quarter results, do you think that the low single-digit percentage growth in sales this year is feasible? This is a bogey that you discussed in the last quarter call. And, if yes, could you just please clarify what gives you confidence on this?



Chris Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO, President*

Well, I will tell you, it is going to be a challenge for us to achieve that low single-digit overall growth rate for the full year for 2014 with the start we had Q1. We were coming off of a nice acceleration in Q4 to our business. Certainly the shallowness of the market here in North America, especially in January and early February, created some real challenges for us. But as we said in our prepared remarks, that we are very confident with the business.

We have got some new product that we are bringing into the marketplace that we think can provide us some opportunities on the top line. I see favorable movements. As much as our European business stepped back a little bit in Q1, we just completed a review of that business and I like the longer-term trend for Europe, certainly on a comparative basis year-over-year.

And we are expecting to be able to drive topline growth into the business in Q3 and Q4. Whether that topline growth will be enough for us to offset the shallowness that has occurred in the business in Q1 will be a challenge for the business.

Kathryn Thompson - *Thompson Research Group - Analyst*

Okay. So then, you noticed in the -- noted in the sector strength focused on maintenance and repair improvement, and this is a trend that we are also seeing reflected in our survey work, and more meaningful improvement in the most recent quarter of our survey. Are you seeing greater relative improvement as the quarter progressed? Just excluding, maybe, the first half that was really more weather-related, but actually moved into second half? And particularly as you look at order rates and just some visibility, what are you seeing in terms of maintenance and repair trends that may be different today than, say, a year ago?

Chris Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO, President*

Kathryn, I think that I'd say two things. I would say that we did identify as maintenance and repair as one of those areas where we are continuing to see some improvements on the year-over-year comp. -- comps. I also would tell you that we would see that within the broader improvements in the business point we look at the business just from maybe the last 5 to 6 weeks where we saw a continuing improving trend in March, as well as maintaining that improvement the first couple of weeks here we have had in April.

So the maintenance and repair side for us, I will tell you, we have got some new technologies into that market that are also providing us some unique opportunities. But we have seen that as an improving segment of the business, improving year-over-year and certainly improving from -- throughout the quarter from early January as we enter into looking at our business today.

Operator

Rob Wertheimer, Vertical Research Partners.

Rob Wertheimer - *Vertical Research Partners - Analyst*

Just wanted to follow up on the sort of bigger picture look at it. You didn't call out weather and I imagine you don't want to get too much into the excuses or whatever, but I'm just curious of whether you do see weather as being impact, whether you could see it in consumables or the type of equipment going into especially in North America, and whether there is not a bounce coming after that.



Chris Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO, President*

You know what, I assured myself I wasn't going to say that word all day on the call. So the market certainly started out much shallower for us in January and early February, especially in our North American business that we had expected. Probably even more surprising because of the acceleration that we achieved in Q4 moving into the business.

But some of that shallowness also was from some of our export business that would not have been impacted by some of those market dynamics here in North America that may have impacted some of the industrials, so a little shallower in our global equipment business than what we expected.

As I said, though, much more aligned with our performance the last 4 to 6 weeks within the business globally, certainly looking more like our prior year trends, but not driving the type of single-digit growth that we were hoping for the business in 2014.

Rob Wertheimer - *Vertical Research Partners - Analyst*

Okay. That was helpful. Thank you. And just your general thoughts again on China; there is a lot of mixed indicators over there. I'm just curious where you think business is headed. Thanks.

Chris Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO, President*

Well, I think there are a lot of mixed indicators relative to the overall market in China, that there are a host of dynamics going on within that particular marketplace. More important is, really, the strategy that we are trying to drive at Lincoln Electric, which is impacting our performance within the business.

So we have been pivoting that business for the last few quarters, trying to drive that business towards higher value-added solution selling and application selling within that market, migrating away from some of the markets which maybe are not as -- not valuing solutions and welding application technologies to where we want to drive that business longer-term. So right now, Lincoln is really experiencing a challenged overall market in China relative to especially heavily industry and a few of the other segments.

But, also, during this dynamic, we are really repositioning that business. Certainly believe that we will continue to experience that in Q2 and hoping to begin to see some improvements as we move towards the back half of this year.

Operator

Walt Liptak, Global Hunter.

Walt Liptak - *Global Hunter Securities, LLC - Analyst*

Vince, I wanted to ask just one last quick one on Venezuela. Given the moving parts for next quarter, do you expect to remain profitable in South America?

Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

Certainly, yes. We expect to remain profitable in South America.

Walt Liptak - *Global Hunter Securities, LLC - Analyst*

Okay. So it is just a degradation to the margins.



Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

Yes. It will likely be degradation to the margin.

Walt Liptak - *Global Hunter Securities, LLC - Analyst*

Okay. Got it. So yes -- and then the North American trends, the tone that I think you guys were reflecting at the end of 2013 was that we were coming out of kind of a slow period and then we had the weather impacts. And I think the expectation was about that we were going to start to get better growth.

So you didn't talk about distributors at all or construction spending or anything like that. Is there anything that you can read through from talking to your customers about, maybe, enthusiasm about the second quarter coming back a little bit?

Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

I would emphasize, Walt, that we did start the year slowly in January and February. The -- March did pick up and our year-over-year comps narrowed significantly. We did have a record equipment sales quarter in the prior year's first quarter, so we had difficult comparisons.

And then, finally, I would add that our domestic business is relatively stable -- flat on a year-over-year basis. Our biggest declines out of North America really came in exports. Our exports declined significantly to China, to Russia, the Middle East, but the bulk of our volume decline in the North American business is really international markets.

Walt Liptak - *Global Hunter Securities, LLC - Analyst*

Okay. Yes. It helps to explain it. Can you help us size that export market for you now?

Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

Yes. Our exports were about \$45 million in the quarter compared to \$69 million in the prior year's first quarter.

Operator

Joe Mondillo, Sidoti & Company.

Joe Mondillo - *Sidoti & Company - Analyst*

My first question, just sort of an overall question. The tone compared to the fourth quarter call seems a little more cautious, which, I guess, is understandable given four of the five segments didn't do so well for the first quarter. However, consumables are two-thirds of the business and they seem to be growing quite well.

First off, what is your interpretation of that? And then secondly, just given the very tough first quarter, especially in North America, with the consumables growing, shouldn't we -- it shouldn't be very likely that we see a pretty good pickup throughout the year.



Chris Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO, President*

Well, I would start, Joe, by saying that it is true that our consumables portfolio is doing a much better than the equipment machines portfolio, save automation. Our automation business is doing well, including the acquisitions.

I will remind you that we did have, we believe, a fairly important pull forward on the equipment side of our business related to engine drive -- the engine drive category because of some new EPA standards that were coming into effect. We haven't seen a rebound in that category and some of our other equipment categories are down compared to the prior year.

Consumables is a good -- strength in consumables is a good indicator that there is industrial activity that is occurring. And the CapEx spend is maybe a separate decision-making process amongst companies in order to replace or add capacity. But, it is not a bad time, certainly, that our consumables are showing resilience in this kind of a market.

Joe Mondillo - *Sidoti & Company - Analyst*

Okay. And then, my follow-up question, related to the greenfield operation in Brazil, I was wondering if you are now able to, or could you quantify for us -- or at least give us a better idea of what kind of savings we are looking at regarding once this project -- or once the operation is completed?

Chris Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO, President*

Sure. I will just give you an update on the project. When I think about the project for our automation business in Brazil, I really don't think of it from a savings perspective as much as a growth perspective. So that business will be -- it is situated outside Sao Paolo.

It is operating. It is meeting with customers. It is taking orders, obviously. The automation business has a very heavy concentration of engineering talent and technical talent needed to do the application work. But that facility is really there to drive that particular market for us as we support our global OEMs that are in Brazil with their automation needs.

So that will continue to ramp up throughout the year. We love the investment. We love it as part of our global automation portfolio. But, certainly, it is not performing at the level that our other automation businesses are at this point. It will continue to build over the next 4 to 8 quarters as we ramp up that business.

Joe Mondillo - *Sidoti & Company - Analyst*

But, once you get that online, there is some initial cost savings just related to the fact that you are not going to be able -- have to export down to that region, correct?

Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

I wouldn't say that -- the strategy behind that greenfield, Joe, in Brazil is not so much a cost savings initiative as a growth platform. It wasn't a tremendous amount of business that could be procured and secured from outside of that country. So it is really a growth strategy and not necessarily an arbitrage on cost.

Joe Mondillo - *Sidoti & Company - Analyst*

Okay. All right. Thanks.



Chris Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO, President*

The opportunity that I see is that, quite frankly, we were selling some product down in that market, but those projects and that floor space now will be utilized to expand the businesses here. So again, to Vince's point, this is really a growth strategy around that expansion.

Operator

Liam Burke, Janney Capital Markets.

Liam Burke - *Janney Montgomery Scott - Analyst*

Chris, could you give us a sense how the quarter progressed in Europe? You showed promise in the fourth quarter and then, obviously, there was a slow start there. But are you seeing any kind of measurable trends as you progress through the first quarter?

Chris Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO, President*

I would tell you that we just finished an operating review with our European team and we are thinking that, quite frankly, we are seeing slightly more favorable trends relative to Europe. Although I believe we have stated, and I still firmly believe, that Europe is going to be on a longer slow growth profile.

We are not expecting the European business and the markets within Europe to necessarily have mid to high single digit growth. We are expecting that maybe we can drive that business to low single-digit growth, but get on a better path.

Now, certainly, some of the challenges economically there from some of the issues with Russia and in that region, we have yet to understand exactly how that may or may not impact some of the economies that are relational to where those activities are. But we believe that our European businesses -- is on the right path. I am expecting low single-digit growth.

We had some real strong activity from some of our alloys portfolio, our Metrode business activities from our [nester] business where we launched several new products at the European [SM] show in the late third quarter, early fourth quarter of 2013.

So we are bringing those products to the market on the equipment side. And, again, I think it is -- I think that we are going to continue to see a long-term improvement in our European business.

Liam Burke - *Janney Montgomery Scott - Analyst*

Okay. And you have spoken a lot about new product introduction for predominantly either technology or innovation of existing products. Are you seeing any competitive responses here or do you think that you are beginning to show a market differentiation strategy here?

Chris Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO, President*

Well, I think Lincoln's been able to show a market differentiation strategy around solutions for a long period of time, and we are just continuing to expand upon that process. So we love some of the new laser hybrid technologies that we are bringing to the marketplace. As I mentioned, we are bringing out a new equipment portfolio for a good piece of the market in Europe, expansion of our alloys technologies. So I really view that as just part of the way we are continuing to drive the business.

Now, there are certainly other global competitors who also bring technologies to the marketplace. But we certainly believe our ability to work with our customers, develop welding and cutting solutions, place us in a leadership role from a technology perspective, and believe that our technology does create a competitive advantage for our business.

Operator

Stanley Elliott, Stifel Nicolas.

Stanley Elliott - Stifel Nicolaus - Analyst

Quick question. Could you guys update us on the net asset exposure and the cash exposure at the re-measured rates? And then maybe talk broadly about concern levels that you guys have about that operation being kind of self-sustaining now that we have gone to the new exchange rates.

Vincent Petrella - Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer

Well, the net monetary asset exposure at March 31, is approximately \$25 million, and the bulk of that is in cash.

Stanley Elliott - Stifel Nicolaus - Analyst

All right. And what about concerns as far as having that being able to operate on kind of a self-sustaining type level?

Vincent Petrella - Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer

We are not concerned about that. The operations remain highly profitable, even with any narrowing of margin contribution moving forward. We fully expect to continue to generate ample cash flows out of that business to fund the working capital and operations going forward.

If we needed to acquire a local denominated debt, we would pursue that. So we don't really have a high level of concern that the operation from a financial balance sheet strength perspective cannot continue to operate into the foreseeable future.

Stanley Elliott - Stifel Nicolaus - Analyst

Great. And switching gears, talking about the automation, is that -- should we still think about that business is kind of being less than 10% of the overall, growing double-digits organically? And then maybe kind of highlight us or update us on kind of what the margin profile of some of those projects are now.

Vincent Petrella - Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer

Well, the product line that we refer to as automation continues to be less than 10% of our overall global consolidated sales. We have talked in the past about the margin profile beginning to exceed our consolidated margin of the Lincoln Holdings organization.

And we have not changed our view that automation will not be a faster growing space within the portfolio of offerings that Lincoln Electric has presently to the market. So we continue to believe it is a double-digit type of growth opportunity for Lincoln.

Operator

Steve Barger, KeyBanc Capital Markets.

Steve Barger - *KeyBanc Capital Markets - Analyst*

Just to follow up on that, the automation question, I hear you saying it is doing better than the traditional welding machines. My question is whether you need to do any more product-centric acquisitions to round out the portfolio or are you more focused on pushing into new geographies now?

Chris Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO, President*

You know, Steve, I would tell you that I think the first focus is probably more geographic. I mean, we have got the greenfield that we have engaged in Latin America and Brazil.

Obviously, a Q4 we announced the Robolution transaction in Europe, although that is a very small start to the footprint there in Germany. So we continue to think that probably the first dynamic that we would be looking at is continued geographic growth.

But, as you saw with Burlington Automation in the fourth quarter where we saw a product that we thought could be very useful tool for the marketplace for 3-D robotic plasma cutting, fits very well within the automation space for people that are building that tool into their factories. There are times where, quite frankly, there are product portfolios that can actually be very additive. And when we see those and can execute on those, we will continue to be aggressive in adding to the automation portfolio.

Steve Barger - *KeyBanc Capital Markets - Analyst*

Got you. And, Chris, in your prepared remarks you talked about new CRM tools and training which should allow for greater sales capacity. Were you really constrained on sales capacity in the past? Or how should we think about how that manifests in terms of driving sales? And what does it mean from a timing standpoint as you roll that out?

Chris Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO, President*

Yes, I wouldn't say that we were constrained. I think it is like any business that continues to try to drive themselves forward with technology and ensuring that we are servicing customers in the best manner. It is just an opportunity for us to make improvements in our processes and tools. And we have implemented those in our North American business as well as utilizing them in a couple of other places around the world like Australia.

But I see it as an enhancement. It is a way for us to continue to allow our people to be productive as well as ensuring that when they are at that point of impact with the customer, they can provide our solutions base to them more effectively. So I didn't see it as a hindrance, but I certainly see it as an enhancement as we install it and move forward.

Operator

Schon Williams, BB&T Capital Markets.

Schon Williams - *BB&T Capital Markets - Analyst*

Vince, you did a good job of holding SG&A flat on a year-over-year basis after adjusting for Venezuela. Just with some of these new product rollouts, or the CRM rollout, maybe the new startup facility in northeast Ohio, I am just wondering, should I expect you guys are still going to be able to keep SG&A flat on a year-over-year basis? Or will some of these new projects start to dial that up?



Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

Our expectation is that SG&A will not ramp up significantly from where we are today.

Schon Williams - *BB&T Capital Markets - Analyst*

Okay. That's helpful. And then just one follow-up on pricing. You have got your annual increase in North America rolling out here in April. I am just wondering, should we expect the normal range of 300 to 400 basis points of pricing in North America? Or given the demand environment, should we expect it to be a little bit more conservative than that?

Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

Our expectation is that pricing will improve in the second quarter. I think 300 to 400 basis points was on the high side. I would say it is going to be a fair amount less than that.

Schon Williams - *BB&T Capital Markets - Analyst*

Okay.

Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

But an improvement on a year-over-year basis. As compared with the first quarter, I would expect some better pricing in the second quarter year-over-year.

Operator

(Operator Instructions) Walt Liptak, Global Hunter.

Walt Liptak - *Global Hunter Securities, LLC - Analyst*

My question is on the Asia-Pacific region. The adjusted EBIT loss there was pretty modest given the drop in revenue. And in your prepared comments, you sort of alluded to some of the things you are doing. I wonder if you could provide some more color on making Asia more profitable.

Chris Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO, President*

Well, I would say a couple things. One is we are not happy with our performance and Asia-Pacific. We have got a lot of resources that we are driving into that region to see if we can make some improvements. But there are a host of businesses within that portfolio.

So we have some areas -- Southeast Asia, Japan, that actually are doing well. We have challenges in our Australian business, primarily driven from some of the compression within the mining sector. We have some bright spots in the region with LNG.

But, really, the important market for us there is our China business. And that is where in my prepared remarks we talked about really repositioning that business towards more higher-value-added applications. And we realized that that is a challenge that we are not going to be able to execute on quickly, but certainly are expecting that we are going to show improvements in that portion of our business as we move into the back half of the year.



Walt Liptak - *Global Hunter Securities, LLC - Analyst*

Okay. Does that also mean you are going to be exiting some lower margin product or increasing pricing?

Chris Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO, President*

Well, you have seen, I think, some compression within the Asia-Pacific region over the last several quarters. And a good bit of that compression has been from us exiting some markets and products that we did not believe were going to meet all our overall goals long-term for the region.

So I would tell you that there is probably a small amount of that to be accomplished, but most of that work is done. Have really been working on the operating model and ensuring that those products and solutions are what our customers are looking for within that market. And I think a lot of that work has been completed and expecting us to show improvement in that market in the back half of the year.

Operator

Mark Douglass, Longbow Research.

Mark Douglass - *Longbow Research - Analyst*

Gentlemen, the big drop in exports, Vince, I think you said that there were some tough comps on the exports in the quarter. When do those -- when do comps for exports, at least, get a little bit easier? And is there any reason to believe that the CapEx spending in these international markets gets better in the second half?

Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

Yes, I commented, Mark, on tough comps as far as the complete equipment portfolio is concerned. And that would also include exports on our international business, since the vast majority of the export business out of the US is on the equipment side. The comps should get a little bit easier in the latter half of the year.

But in terms of predicting when China might turn, which had some of our biggest declines in export business in our portfolio, as well as Russia and some parts of the Middle East, as your guess might be guess as good as ours.

Mark Douglass - *Longbow Research - Analyst*

It always is, right?

Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

Yes. But your guess is probably better.

Mark Douglass - *Longbow Research - Analyst*

Okay. So the run rate -- the \$45 million run rate is probably a decent place to start, then?



Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

Yes, I would think so.

Mark Douglass - *Longbow Research - Analyst*

Okay. And then, housekeeping, the effective tax rate on the adjusted basis -- looks like it was about 26%. Is that correct?

Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

On a reported basis, it was 31% and change. I don't know what you're adjusting for.

Mark Douglass - *Longbow Research - Analyst*

Well, your adjusted EPS, the \$0.91.

Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

Okay.

Mark Douglass - *Longbow Research - Analyst*

It looks like it's actually 26%, but is it, going forward, 31%?

Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

Yes. So we have booked on a reported basis 31%. So at this point in time, early in the year, based on our forecast of the geographical earnings spread and the statutory rate applied to those, we would tell you that that is as a good a rate as any to use at this point in time, somewhere around 31% to 32%.

Operator

I would like to turn the call back to Vincent Petrella for any closing remarks.

Vincent Petrella - *Lincoln Electric Holdings, Inc. - SVP, CFO, Treasurer*

Thank you, Danielle, and thank everyone for joining us on the call today and your continued interest in Lincoln Electric. We very much look forward to reporting our progress during the second quarter call that we will schedule towards the end of July. Thank you again and talk to you then.

Operator

This concludes today's teleconference. You may now disconnect your lines at this time and thank you for your participation.



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