THOMSON REUTERS STREETEVENTS

EDITED TRANSCRIPT

LECO - Q4 2017 Lincoln Electric Holdings Inc Earnings Call

EVENT DATE/TIME: FEBRUARY 14, 2018 / 3:00PM GMT

OVERVIEW:

Co. reported 4Q17 reported operating income of $75.5m and diluted EPS of $0.36.

CORPORATE PARTICIPANTS

Amanda H. Butler *Lincoln Electric Holdings, Inc. - VP of IR*

Christopher L. Mapes *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

Vincent K. Petrella *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

CONFERENCE CALL PARTICIPANTS

James Giannakouros *Oppenheimer & Co. Inc., Research Division - Executive Director and Senior Analyst*

Jason Andrew Rodgers *Great Lakes Review - VP*

Joseph O'Dea *Vertical Research Partners, LLC - VP*

Liam Dalton Burke *B. Riley FBR, Inc., Research Division - Analyst*

Mircea Dobre *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Nathan Hardie Jones *Stifel, Nicolaus & Company, Incorporated, Research Division - Analyst*

Saree Emily Boroditsky *Deutsche Bank AG, Research Division - Research Analyst*

Seth Robert Weber *RBC Capital Markets, LLC, Research Division - Analyst*

Walter Scott Liptak *Seaport Global Securities LLC, Research Division - MD & Senior Industrials Analyst*

PRESENTATION

Operator

Greetings, and welcome to the Lincoln Electric 2017 Fourth Quarter and Full Year Financial Results Conference Call. (Operator Instructions) And this call is being recorded.

It is now my pleasure to introduce your host, Amanda Butler, Vice President of Investor Relations and Communications. Thank you, you may begin.

Amanda H. Butler - *Lincoln Electric Holdings, Inc. - VP of IR*

Thank you, Takia, and good morning, everyone. Welcome to Lincoln Electric's 2017 Fourth Quarter Conference Call. We released our financial results earlier today, and you can find our release as an attachment to this call's slide presentation as well as on the Lincoln Electric website at lincolnelectric.com in the Investor Relations section.

Joining me on the call today is Chris Mapes, our Chairman, President and Chief Executive Officer; as well as our Chief Financial Officer, Vince Petrella. Chris will begin the discussion with an overview of our full year results, and Vince will cover the quarter performance in more detail. And following our prepared remarks, we're happy to take your questions.

Before we start our discussion, please note that certain statements made during this call may be forward-looking and actual results may differ materially from our expectations due to a number of risk factors. A discussion of some of the 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.

In addition, we discuss financial measures that do not confirm to U.S. GAAP. A reconciliation of non-GAAP measures to the most comparable GAAP measure is found in the financial tables in our earnings release, which again is available in the Investor Relations section of our website at lincolnelectric.com.

And with that, I'll turn the call over to Chris Mapes.

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

Thank you, Amanda. Good morning, everyone. We capped off 2017 with solid top line momentum and record or near record performance across many key financial, operational and environmental metrics in our legacy Lincoln Electric business. These achievements advance us towards our 2020 Vision and Strategy goals, and we are well positioned to capitalize on accelerated growth and superior value creation in 2018.

Before I discuss our financial results, I would like to thank and congratulate our employees for achieving an all-time record performance for safety and record achievement in our global environmental metrics in 2017. Great work.

Now looking at our 2017 results. Sales, excluding Venezuela, increased 16% to $2.6 billion from 7% organic and 8% acquisition growth. Our strategic focus on mix and diligent pricing management help mitigate the impact of raw material inflation. Margin compressed as our commercial teams continued to implement pricing actions to recover the frequent raw material cost increases that we have been incurring globally.

I'm pleased to report that excluding acquisitions, our adjusted operating income rose 12%, and we expanded our margin by 50 basis points to 14.7%. This yielded a 22.2% incremental operating income margin for the year while continuing to invest in the business.

Reported diluted earnings per share was $3.71. Excluding special item charges, adjusted EPS increased 15% to $3.79.

We generated $335 million in operating cash flows, driven by a record 14.2% average operating working capital ratio in our legacy Lincoln Electric businesses. This yielded a 108% free cash flow conversion of adjusted net income.

ROIC remains solid at 16.2%, and we continued our 23-year track record of consecutive dividend increases with an 11% increase to our 2018 dividend payout rate.

Moving to Slide 4. Industrial demand firmed and accelerated in the fourth quarter. Our organic sales increased by 10%. We achieved good organic growth across all of our reportable segments, geographic regions and U.S. exports.

By product area, both consumables and equipment solutions increased at a double-digit rate and automation increased at a mid-single-digit rate despite challenging prior year comparisons.

Approximately 95% of our revenue is exposed to end markets that are now growing. Early 2018 sales trending suggest accelerating global industrial demand. We continued to expect mid- to high single-digit percent organic sales growth in 2018 as markets accelerate and we benefit from exciting new product launches later this year.

With growth, we're also expecting raw material inflation to persist in 2018. Our commercial teams are implementing pricing actions to offset the unfavorable impact, but these actions will result some choppiness in margin results as the inflationary environment continues to progress.

Moving to Slide 5. I'm pleased to report that our cross-functional integration teams have made tremendous progress in the last few months, shaping the European Lincoln Electric and Air Liquide Welding businesses into one company, one team, under one strategy. While this is a multiyear program, we are enjoying a strong start and faster implementation than initially expected. We remain confident that we are on track to deliver our targeted synergies of $30 million.

Our fourth quarter to mid-February progress covers a wide range of operational and commercial initiatives from platform consolidation announcements to procurement savings, system integrations and commercial alignment.

After returning from Europe 2 weeks ago, I was pleased by the commercial success we've already secured by leveraging key technologies in brands like Oerlikon with our Lincoln Electric products. The combination is providing us with a competitive advantage that we will continue to capitalize on and build upon in 2018.

We incurred $5.5 million in rationalization charges in the fourth quarter with minimal cash costs. While we expect to fully recognize the benefit of our integration actions in the second half of 2018, the team's accelerated pace has increased EPS accretion to $0.04 to $0.05 of EPS per quarter in the first half of 2018.

Before I pass the call to Vince, I'd like to thank the organization for their successful execution of our strategic initiatives, supporting the Air Liquide Welding acquisition and integration activities and continuing to prioritize our customers first.

In 2017, we truly demonstrated the strength of our 11,000 employees, who are committed to doing their best each day for Lincoln Electric. And we will continue to work diligently to execute on our 2020 Vision and Strategy. And now I'll pass the call to Vince.

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

Thank you, Chris. Looking at our fourth quarter income statement highlights on Slide 6, our consolidated fourth quarter sales increased 32.5% on 6.8% volume growth, 3.2% higher price, a 20.3% benefit from the Air Liquide Welding acquisition and 2.2% from favorable foreign exchange translations.

Our fourth quarter gross profit margin declined 300 basis points to 32% as compared with 35% in the prior year. The decline primarily reflected the addition of Air Liquide Welding and a $2.3 million charge from the amortization of the step-up in the value of acquired inventories from this transaction.

Excluding the acquisition and special items, gross profit margins were 33.8% or 120 basis point decline versus the prior year on unfavorable price cost due to the raw material inflation, including a $1.5 million LIFO charge in our Americas Welding segment and unfavorable product sales mix.

Our SG&A expense increased 33% to $152.6 million or 20.4% of sales due to the addition of Air Liquide Welding and acquisition-related expenses. Excluding the acquisition and special items, SG&A expense increased 9% to $124.4 million. The increase was primarily due to higher incentive compensation, charitable contributions and wage costs. SG&A, as a percentage of sales, excluding these items, declined 60 basis points to 19.7% on improved sales leverage.

In the fourth quarter, we incurred several special items that are listed on Slide 7. These items included a $2.9 million noncash pension settlement charge related to lump-sum payments from our U.S. defined benefit pension plan; rationalization and asset impairment charges of $6.6 million, primarily from our European integration activities; a net $1.9 million bargain purchase adjustment as we continued to finalize our Air Liquide Welding purchase price allocation; and a $3.6 million charge for acquisition transaction and integration costs.

Now turning back to Slide 6. Reported operating income declined 9.1% to $75.5 million or 10.1% of sales. Excluding special item charges, adjusted operating income increased 11.7% to $92.8 million or 12.4% of sales. Excluding the acquisition and special items, adjusted operating income would have been $89.6 million or 14.2% of sales. A 50 basis point decline versus the prior year period due to unfavorable price cost, higher incentive compensation cost and increased charitable contributions.

Our fourth quarter effective tax rate was 67.2% compared with 31.7% in the prior year period because of the $28.6 million charge associated with the U.S. Tax Cuts and Jobs Act. This charge primarily relates to taxes on the company's unremitted foreign earnings and profits.

Excluding the charges related to the U.S. Tax Act, our fourth quarter tax rate would have been 25.8%. The lower adjusted effective tax rate is due to the geographical mix of earnings and the favorable effect of discrete tax items, including deductions related to stock option exercises.

In 2018, our effective tax rate is expected to be in the low to mid-20% range subject to the future mix of earnings and the timing and extent of discrete tax items, including stock option exercises.

Fourth quarter diluted earnings per share decreased approximately 56% to $0.36 per share compared with $0.81 in the prior year. On an adjusted basis, diluted earnings per share increased approximately 25% to $1.01 on higher organic sales.

Now let's move to the geographical segments on Slide #8. Americas Welding segment's fourth quarter adjusted EBIT dollars rose 4% to $74.5 million. The adjusted EBIT margin declined 140 basis points to 16.8% on higher incentive compensation cost, charitable contributions and rising raw material cost against a difficult comparison in the prior year.

Demand strengthened through the end of the quarter across most end markets and generated double-digit volume growth in both consumables and equipment. Americas segments top 3 end markets, automotive, heavy industries, general industries, increased at a mid-teens percent rate as did the automation portfolio.

Moving to Slide 9. The International Welding segment adjusted EBIT increased 61.2% to $12 million due to the addition of Air Liquide Welding, sales leverage in Asia Pacific and for favorable foreign exchange. Adjusted EBIT margin declined 90 basis points to 4.6% because of the acquisition. Excluding the acquisition, adjusted EBIT margin was 5.6%, a 10 basis point improvement versus the prior year.

Organic sales increased 3.1% with 5.6% higher price and a 2.5% decline in volumes due to lower sales in energy-related end markets and a challenging prior year comparison.

Moving to the Harris Products Group segment. Fourth quarter EBIT margin improved 270 basis points, 12.9% on approximately 7% higher volumes. All segments and geographies grew in the quarter, reinforcing broadening improvement in end markets.

Moving to Slide 11. We generated strong cash flows in the fourth quarter of $89 million with a 99% cash conversion of adjusted net income. On a full year basis, we achieved $335 million of cash flows from operations on a solid 108% cash conversion ratio. We also achieved record working capital efficiency with the 14.2% average operating working capital ratio in the legacy Lincoln businesses. This performance exceeds our 2020 goal of 15%.

Moving to Slide 12. We spent $72 million towards acquisitions in the year and invested $62 million in capital expenditures to support key projects such as our new welding technology and training center. Looking ahead to 2018, we estimate full year capital spending to be in the range of $60 million to $70 million.

During the fourth quarter, we continued to return cash to shareholders, paying cash dividends of $23 million, reflecting the 9% increase in the dividend payout rate. In December, the board approved an additional 11.4% dividend rate increase for 2018. We also spent $20 million on repurchasing approximately 222,000 shares in the open market during the quarter. Our full year 2017 repurchases were $43.2 million. And we expect to maintain a balanced capital allocation strategy in 2018, prioritizing growth investments and returning cash to shareholders through our dividend program and share repurchases.

That's the extent of our prepared remarks. I'd like to now turn the call over to questions. Takia?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of Joe O'Dea with Vertical Research.

Joseph O'Dea - *Vertical Research Partners, LLC - VP*

First question is just a little bit of clarification. You commented on some choppiness, I think, within margins over the course of the year related to pricing plans in some of the raw material inflation you're looking at. And any clarification or additional details on how you foresee that playing out whether that's first half margins versus second half margins, put some of the timing sensitivity there?

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

Right. So I think it's difficult to predict the timing of continued raw material and inflationary increases. I think we are confident based on what we've seen over the past 6, 9 months and what our expectations are for 2018, including what we're seeing from a volume perspective across our businesses and our customers' businesses that we will continue to see inflation progress as the year unfolds. We're just cautioning our investors and analysts to understand that there could be, from a quarter-to-quarter basis, some volatility and choppiness and lags and following price increases with these inflationary increases in our business that are coming more rapidly. But I would say Joe that from an intermediate longer-term perspective, we still are confident that we have a business model that can deliver 20% to 25% incrementals on a pretty consistent basis. But we're just cautious that 2018 will be represented by a more rapid inflationary increases and Lincoln response to that could result in some choppy incrementals from quarter-to-quarter.

Joseph O'Dea - *Vertical Research Partners, LLC - VP*

I appreciate it. And then in terms of flexibility on pricing and pricing into customer channels, could you talk a little bit about how you anticipate pricing into the distribution side versus pricing into the end-user side? And whether as we're seeing the strengthening in end markets, the pricing kind of leverage that you have in the end users, do you see that strengthening a little bit?

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

Well, certainly, we'd expect that strengthening market creates an easier environment for us to move forward with raw material increases into that particular space. I think a couple of key points is that if this is a global impact. So we're seeing this inflationary impact in a multitude of markets. And obviously, we participate in a multitude of segments. So we need to see the strength in all of various segments for us to be able to work with those customers to understand the value that Lincoln's creating and being able to move those material cost increases into the market. When we're dealing with our channel partners, obviously, that's a different conversation. They're working with a multitude of our joint customers. And there are times when it is easier for that to move through because the consolidation of that customer base and with that channel partner creates one conversation for us with the channel partner. But obviously, we'll continue to work with them. And our message, again, is that we expect to continue to see inflation in our global business as we move throughout 2018 and still have very confidence in our ability to move that inflation to the marketplace over the longer term.

Operator

Our next question comes from Jason Rodgers with Great Lakes Review.

Jason Andrew Rodgers - *Great Lakes Review - VP*

Yes, I just wanted to follow up on the price increases in raw material costs. I was wondering what the net impact in the quarter was on -- from higher raw material cost net of price increases? And what -- and if you are seeing that raw material costs are accelerating here in the first quarter?

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

Yes, Jason. So our estimate of the price cost impact on margin in the fourth quarter was a decremental impact to about 70 basis points from price cost. We continued to see raw input costs rise through the end of the quarter and into 2018. We will be moving additional price increases into the market during the course of the first quarter. And our expectations are that we will still have some decremental impact in the first quarter. But that 70 basis points gives you some indication of the impact on fourth quarter results.

Jason Andrew Rodgers - *Great Lakes Review - VP*

All right. And what percent of your debt is fixed currently?

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

Right now, it's about 80% to 85% fixed.

Jason Andrew Rodgers - *Great Lakes Review - VP*

Okay. And you've raised your accretion estimates for Air Liquide Welding here in the first half. Is it just a function of faster execution on the cost synergies? Or are you funding additional synergy opportunities?

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

I would say both. I -- Vince and I have just returned back from Europe a couple of weeks ago. And meeting with our teams on the integration review, we're very excited about the progress we're making. We're finding opportunities that we didn't plan on initially. And some of the opportunities we can execute on earlier. Some of those opportunities will be pushed out some as we prioritize the actions with the teams. But still extremely excited about the progress our teams are making and the opportunity that we see with the merger of those businesses as we're moving forward.

Operator

Our next question comes from Nathan Jones of Stifel. Our next question comes from the line of Saree Boroditsky with Deutsche Bank.

Saree Emily Boroditsky - *Deutsche Bank AG, Research Division - Research Analyst*

You talk -- can you talk a little bit about the benefit from Air Liquide in the quarter from a top line perspective? The day came in higher than you guys were expecting, how much of that was FX versus volume?

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

Well, in the quarter, Air Liquide contributed about $112 million of top line revenue. And so there is really no translation effect to that because they weren't in the prior year, right? So there wasn't an impact from a weaker dollar on the acquisition revenues. But we did have a foreign exchange translation improvement in the overall business of $12 million or about $9 million, $10 million in the International segment.

Saree Emily Boroditsky - *Deutsche Bank AG, Research Division - Research Analyst*

Okay, that's helpful. And then could you provide some color on what you're seeing in the energy market? There has been some positive development around the North Sea recently. So I was just wondering if you were seeing any improvement quarter-to-date on the International side?

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

Well, I wouldn't say anything necessarily quarter-to-date on the International side. I will share with you that I recently returned from business reviews in Asia and Southeast Asia, specifically. And there was more optimism around there being activity in the offshore market and offshore construction. So I believe that energy in total is positive, although I will tell you we had a challenging comp in our International segment with a portion of energy. Portion of that was a very difficult comp from prior year and probably project work. But I think offshore is beginning to show some activity, probably not enough energy or activity behind that yet to say that it's trending, especially when we talk about the offshore segment of energy.

Operator

Our next question comes from Nathan Jones of Stifel.

Nathan Hardie Jones - *Stifel, Nicolaus & Company, Incorporated, Research Division - Analyst*

All right. Can you hear me now?

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

I can hear you now.

Nathan Hardie Jones - *Stifel, Nicolaus & Company, Incorporated, Research Division - Analyst*

Awesome. Vincent, you talked a little bit about expecting some choppiness in incrementals, over the medium to long term would expect 20% to 25% incrementals. Do you expect to be able to do that for the full year in 2018 if we may take some of the quarter-to-quarter choppiness out?

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

Yes. Look, I would think so. We did a 22%, I believe, incremental margin for all of 2017. We did have some fairly rapid inflationary increases during the course of the year. I think we'll see more of that in 2018. I think there are some other positive drivers, including Air Liquide Welding integration that should give us an upside on our incrementals. I think we're going to have some more downside challenges though based on what we see in the inflationary environment. But I think if you're looking at a rolling 4 quarters, I'm pretty confident that if you put 4 quarters together, we ought to be in that kind of a range.

Nathan Hardie Jones - *Stifel, Nicolaus & Company, Incorporated, Research Division - Analyst*

Okay. And then just a little bit more on Air Liquide maybe in terms of working capital, where is that relative to where Lincoln is? Do you think you can get them to the same place you are? How much cash could that actually produce out of the business?

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

That's a great question. So we -- as we stated in our prepared remarks, we ended up at 14.2% average operating working capital in the legacy business, Nathan. If you blend in Air Liquide, we're 15.9%. So it's a 170 basis point deterioration in the consolidated totals. We have already freed up $17 million in inventory during the course of the 5-month period that we've owned the business in 2017. We think that 2018 we can replicate that and achieve an even greater improvement in inventory and working capital management. So we're optimistic that there are good opportunities to align Air Liquide Welding's acquired business with Lincoln's. And we think that, that $17 million can be replicated and perhaps exceeded during the course of 2018. Be mindful of the -- low-hanging fruit is the first areas that will be focused on. It will become more difficult as we own the business, but I think there is lots of opportunity to bring them in line with Lincoln's expectations in that regard.

Nathan Hardie Jones - *Stifel, Nicolaus & Company, Incorporated, Research Division - Analyst*

And then I know everybody would be focused on the cost synergy between the 2 businesses, but could you maybe talk about some of the opportunities you see on the revenue synergy side between the 2 businesses?

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

Yes, I think the best way to give you it would be an example of that. We're recently doing a trip to Southeast Asia. I had an opportunity to visit with one of the larger distributors for the Air Liquide business. And although, most of that business was driven from core Europe, they did have a handful of distributors that were providing their products to the markets globally. And during that visit, an excellent opportunity to talk to them about their perspective of the brand and the technologies. But I also got the chance to see how our teams were working with them and that particular channel partner now is bringing in Lincoln Electric equipment to complement the Air Liquide Welding consumables that they've been buying. And my expectation is that, that particular incident, we're going to be able to replicate in a multitude of channels and with a multitude of customers around the world. And I was very excited about the execution of that, and we'll continue to drive that as we move throughout 2018.

Nathan Hardie Jones - *Stifel, Nicolaus & Company, Incorporated, Research Division - Analyst*

There's no numbers you could point in that way at this point?

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

Well, that particular customer was -- is probably going to be on an annual basis for equipment less than $1 million, but it will be a material order. So at this point, our teams aren't ready to be able to identify the amount of leverage we will be achieving from that, but I've got great confidence in it. We'll try to provide more guidance on that as we're moving forward.

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

Jason, I would just only add to that, that any improvement in revenues will likely be offset by our desire to reshape the combined business towards a more attractive mix and richen the opportunity for margin improvement. So to the extent that we do have wins or improvements and synergies at the top line, I do fully expect that there will be offsets as we consolidate the platforms and we move our manufacturing platform around and integrate the businesses. It's likely that the low end are the businesses that we view as a little less attractive will have a declining impact on sales as well.

Operator

Our next question comes from Jim Giannakouros with Oppenheimer.

James Giannakouros - *Oppenheimer & Co. Inc., Research Division - Executive Director and Senior Analyst*

Sticking on the International sales, you decided tough comps. Was there any disruption to sales from the ALW integration? If I recall, you're making some changes on go-to-market strategies or just your sales effort there.

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

We just completed some reviews of that business. I mean, whenever you have this type of a large merger, there is certainly some risks associated with that. But I can't identify any challenges that we've had relative to supplying product to our customers or alignment with our teams. I was very happy with our results and don't believe we've had any of those negative impacts within the business or the portfolio.

James Giannakouros - *Oppenheimer & Co. Inc., Research Division - Executive Director and Senior Analyst*

Okay. And automation, again, you decided tough comps, but you did grow mid-singles. What were the sales in both 4Q and FY '17? And do you have an outlook for 2018 as far as that bucket globally?

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

The run rate in 2017's fourth quarter was roughly $100 million. And so I think we're going to -- we expect a mid- to high-single-digits growth rate in 2018 from that.

James Giannakouros - *Oppenheimer & Co. Inc., Research Division - Executive Director and Senior Analyst*

Okay. And one more, if I may? Price actions, I can appreciate choppiness. You're not the only one who's taking the price action. My impression is that they're decently received if you can comment on. Did you get all the price that you anticipated in -- with your November price increases? Were they concentrated in consumables or in equipment? And also just any color on if steel stays where it is, you anticipate to fully offset some time this year? And if yes, when?

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

Well, I think the important comment would be that we expect to be able to continue to take raw material increases and move those increases to the marketplace effectively. That's what we've been able to do here at Lincoln Electric for a long period of time. And go and work with our customers and ensure them that our solutions are going to add value to them in their business, and our teams are working diligently to ensure that we accomplish that. As I mentioned earlier, it's difficult to talk about any one particular increase, one we don't really like to talk about pricing in that type of granularity. But as importantly, this is a global phenomenon that we're dealing with and any comment I might make around one region might not be representative around the global impacts that we're seeing. I really think the important message is our confidence in being able to work with the markets and work with our customers to recover the cost increases that we're seeing with raw materials, accepting that because of timing and acceleration of those that we may have some choppiness as we're executing on that throughout '18.

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

And then in terms of, Jim, the split between consumables and equipment. Clearly, the price increases are much greater on the consumable side because of the raw input costs associated with steel and other commodities. And so the bulk of our increases that you see on our pricing lines for the Americas Welding and International Welding segments are really focused on the consumables product lines.

Operator

Our next question comes from Walter Liptak with Seaport Global.

Walter Scott Liptak - *Seaport Global Securities LLC, Research Division - MD & Senior Industrials Analyst*

I want to ask about the tough comps in International. And if you could just refresh our memories on what was it about the fourth quarter last year I guess related to energy that was so strong? And then as you think about comps in 2018, it doesn't look like you have any of those big volume spikes in 2017. Do you expect to see volume growth in 2018?

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

Right. So we did have 2 end markets that were down in 2017's fourth quarter for International was really energy-related markets, offshore. We had a nice quarter last year, and we're down significantly on a year-over-year basis, as well as pipe mills, which were down as well in the 2017 quarter. So that's where we saw the bulk of the change. Also Asia Pacific, it was much stronger as well in volumes in the prior year.

Walter Scott Liptak - *Seaport Global Securities LLC, Research Division - MD & Senior Industrials Analyst*

Okay. The pipe mill part of it, it sounds like oil and gas is ramping up for welded pipes. Why you think it was down during the fourth quarter? Was it just a timing issue or shutdowns?

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

It's very project oriented. Also the timing of projects that hit the quarter can flip between quarters during the course of the year. So we're not too excited about a down quarter in these types of project-oriented industries. We do see that, for example, offshore was up in the Americas region. So we think that in 2018, we all see a better result in International offshore and pipe mills and maybe what we saw in one individual discrete quarter.

Walter Scott Liptak - *Seaport Global Securities LLC, Research Division - MD & Senior Industrials Analyst*

Okay. Got it. And if I can just ask one on the price cost too. Just looking at the pricing numbers that you guys put out in Americas up 2.9% and International 5.6%, that's a pretty good pricing. I think it's probably the best I've almost ever seen. So just to be clear, what you're saying is cost coming up faster than pricing and this is largely a timing issue that we're dealing with.

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

That's correct. And I think these are some of the bigger pricing increases that we've seen in some time. But the increases are fairly rapid and sizable. And we're following behind those with price increases that do take some time to put into the market through our channel partners and end customer users. So they are fairly sizable cost increases that we're experiencing in raw inputs and other inflationary items.

Walter Scott Liptak - *Seaport Global Securities LLC, Research Division - MD & Senior Industrials Analyst*

All right. And the volatility that you're talking about is just raw materials come up, there is a lag. I wonder if you can talk about what that lag typically is in a month, 2 months?

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

It really varies. It depends on the relationships. You could have situations where there is longer-term contracts with customers. You could have situations that you need to have individual negotiations. And so it varies depending upon the region, the customer, the channel. But I would tell you that it can take 3, 4 months to accomplish complete pricing change when you're trying to move price into the marketplace on a global basis.

Walter Scott Liptak - *Seaport Global Securities LLC, Research Division - MD & Senior Industrials Analyst*

Right. Okay, great. And just switching gears to the comment that you made about the low-hanging fruit in Air Liquide Welding. I wonder if you could talk about where -- what is the low-hanging fruit that you're seeing? And what's moving along faster on the synergies? It's great to see but I wonder if you could provide some details on that.

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

Yes. So we're probably ahead on synergies as our -- in the purchasing area being able to identify areas where we can achieve lowest cost and highest quality vendor relationships. I think we're ahead on our ability to announce and start to work on some manufacturing and distribution consolidations. I think we're certainly ahead on trying to run the business in an integrated way. And -- so I -- these are all things, Walt, at least identified, and we knew that we'd be working on from the time we announced this transaction back in last March. And just that I think we've been a little bit more effective and we've moved faster than what we anticipated to try to bring some of these synergistic opportunities forward into the front half of 2018 rather than the back half. So I think our teams in all work streams and all areas are more successful than what we had originally had anticipated at this point in time. There's still a tremendous amount of work to be done, but we're optimistic -- Chris and I are optimistic that we're going to be on track for and perhaps even bring forward a little bit earlier this -- the savings that we had identified from the outset.

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

Walter, as an example, we've already developed the strategy for the commercial teams. Merged the commercial organizations underneath one leadership team and our -- have already completed that piece. And as Vince mentioned earlier, I'm very happy with our ability to drive $17 million of working capital out of that business in the first 5 months. And we believe there are further opportunities for us to improve the working capital efficiency as we move forward.

Walter Scott Liptak - *Seaport Global Securities LLC, Research Division - MD & Senior Industrials Analyst*

Okay. Yes, it sounds great. Congratulations with that. Given what you said, is there a chance that you get more accretion in 2018 as these things -- these programs move faster?

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

I think there is -- I think we're -- we need to wait though, Walt, to see how this forms up at the end of the first and second quarter. And there is certainly that opportunity, but we'll need to see that the execution that we have laid out for the first half of the year continues to be ahead of schedule. And I think we're -- we'll wait until maybe the first half is in the book to look at that again on whether or not that $30 million and whether or not the $0.06 per quarter can be revised.

Operator

Our next question comes from Seth Weber with RBC Capital Markets.

Seth Robert Weber - *RBC Capital Markets, LLC, Research Division - Analyst*

I wanted -- could you dig in a little bit to the double-digit strength that you're seeing in the automotive and transport segment? I mean, is that coming from new platforms? Is that type of growth sustainable or whether some kind of one-off e-sales this quarter?

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

Well, it's really not driven by any one-off. I think if you take a look at our performance throughout 2017, we had a couple of quarters where we were performing better in that particular segment than maybe what the broad market dynamics were. We've had some new technologies that we brought into that segment over the last 6, 12, 18 months. So I certainly think is benefiting us. We've also found a couple of opportunities where we can expand our presence with global OEMs by providing them some support in other regions where we may be weren't providing that previously.

So I don't see any one-offs as it relates to the quarter. And I think this is just a continuation of some of the success that we've had in that segment as we trended through 2017.

Seth Robert Weber - *RBC Capital Markets, LLC, Research Division - Analyst*

Okay. So you would expect segment growth there to continue to outpace the build -- auto build levels?

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

Yes.

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

Yes. So that's been the case during the course of all of 2017 and it's just expanding in 2018. So this is not -- in this particular case, this is not a discrete quarter of performance. We have a track record of several quarters now in a row outperforming what the builds would suggest.

Seth Robert Weber - *RBC Capital Markets, LLC, Research Division - Analyst*

Sure. Okay. And then Vince just a clarification, I think. I think I heard you call out incentive comp in the fourth quarter for the Americas margin. I guess, can you quantify that? And is that -- does that go -- become a tailwind in 2018 when we started looking at year-over-year comparables?

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

Yes. So I estimate that we took additional $4 million charge in the Americas and actually globally for incentive compensation over and above what might have been a normal provision for the profitability of the business on a year-over-year basis. So the prior year was probably little light. The current year was a little heavy. And so we had a $4 million delta that burdened the fourth quarter as compared to the prior year's fourth quarter. So it should be a little bit of a tailwind on a quarterly basis in 2018.

Operator

The final question in queue comes from the line of Mig Dobre with Baird.

Mircea Dobre - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

So just want to go back to volumes in America, which were great. They were much better than, I guess. And I think Vince thinking back at our conversation last quarter, they were maybe better than what you were thinking as well since things picked up sequentially in spite of the tougher comps. So I guess, I'm wondering, what in a quarter may be worked out better than what you initially envisioned from a volume perspective?

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

Actually, the increase was across both equipment and consumables. So we had a really a double-digit improvement in both categories. We also outperformed on the automation side of the business. You might recollect since you are reminding me of what I said in the third quarter, you might also recollect that we're a little concerned about the third quarter trends in the automation business. And actually, automation picked up and became stronger and was less of a drag than what we had anticipated at the end of the third quarter. And as Chris stated in his comments, that strength has carried over into the 2018. So we're now optimistic that our order trend levels will be very positive in that product lines segment in

2018. So just to summarize, Americas was strong across both consumables and equipment. More of those end markets picked up across the board. Heavy equipment manufacturers, automotive, we just had a very nice broadening of end markets during the course of the quarter.

Mircea Dobre - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

That sounds great. And I think Seth tried to get at this in terms of automotive and transportation. You said, you expect to grow in excess of builds. But when you kind of look at Chris's comments for mid- to high single-digit organic growth in '18, how would you think about your growth in this market versus that guidance specifically?

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

Well, in the quarter, it was up by double digits on a global basis, up stronger in the Americas and internationally. But I think that's going to be challenging to replicate. We do have the comparisons that come around in the second half and the fourth quarter of this year that will make that kind of number difficult. But we're -- at least, I'm optimistic that we're going to see good outpaced growth in automotive and transport compared to the build just based on our historical experience, our penetration in the automation product line, the new products that Chris mentioned in his comments. So I think we're -- I'm comfortable with Chris's guidance that we're going to be mid- to high single digits in that area.

Mircea Dobre - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Okay. And then, lastly, I was trying to run some quick math just based on your comments on the 70 bps headwind from price cost and you're pricing that you reported. And I'm guessing that raw materials are something like 20% of sales? I don't know if I have this right. And related to this 2, when you're thinking about your cost more broadly, is there anything else other than steel that we need to be aware of as we think about '18?

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

Well, there is a lot of things other than steel that you should be aware of. And my view of that is that steel is our biggest input cost, Mig. And so we're very focused on that because it represents hundreds of millions of dollars of our COGS and our spend. But we're seeing inflationary increases across the board. Chemicals are a big purchase component. We buy electronics and engines. And we buy lots of different commodities, if you will. And so I think that inflationary comment extends across all of our inputs, including frankly, wages and salaries and compensation costs will continue to rise, we believe, in 2018 at a faster pace than what we've seen for the last several years. But your assumption of 20% I think is rather low. It's a much higher number than 20% is raw inputs.

Mircea Dobre - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

It is. Okay. And one more and then I'm done. When I'm looking at your reported pricing stat in International versus the Americas. Is there any color to provide in terms of why maybe you've gotten a little more price in the International? Anything to be gained there?

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

No, we've just been more aggressive there because we feel that there is more business and products that are being sold at prices or margins that we view as being less attractive than our objectives from a global perspective. So we're being a little bit more aggressive to manage perhaps out some of the less attractive business that we have in our International portfolios. So it's a matter of margin and portfolio management from an International perspective.

Operator

Our last question comes from the line of Saree Boroditsky with Deutsche Bank.

Saree Emily Boroditsky - *Deutsche Bank AG, Research Division - Research Analyst*

With over $500 million of cash in marketable securities at year-end, it seems like you could end up in the net cash position by the end of 2018. So could you just touch on your leverage target? And then how you're thinking about using that excess cash?

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

So we think about our capital allocation and debt targets from a debt-to-EBITDA perspective. We'd like to have that number in the short intermediate term at somewhere between 1.25 and 2x debt to gross -- gross debt-to-EBITDA. So we fully expect to continue to follow our capital allocation plan to find those capital investments that make sense from both a strategic and return perspective where we will continue to raise our dividend in the foreseeable future at a double-digit pace, high single-digit double-digit base. And we will continue to buy shares to maintain our share count so that the wild card, frankly, is what we are able to source in the M&A arena that can use that very strong balance sheet and cash on the balance sheet for growth and advancing our strategic initiatives in our 2020 Vision.

Operator

And our final question in the queue comes from the line of Liam Burke with FBR.

Liam Dalton Burke - *B. Riley FBR, Inc., Research Division - Analyst*

Chris, on the automation side, you seem that it had been making nice progress on penetrating the market. Have there been any change in the competitive response?

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

No I really can't point towards any real change in the competitive response. We're very focused on executing that longer-term strategy that we've laid out for our automation business. I still see or I still and very confident in the long-term trends towards automation. And as we mentioned before at Lincoln, we want to attack those long-term trends in 2 manners. We want to build our education model to train and develop the new welder and that's the investment in our new welding and training technology center here at our campus in Cleveland. And that's also providing automated solutions to the global marketplace. And we believe that trend continues strongly and that it's a long-run trend, a multiyear trend. And we're going to continue to invest behind it and identify other ways for us to expand the business whether through greenfields, M&A or other opportunities for us to expand within automation.

Liam Dalton Burke - *B. Riley FBR, Inc., Research Division - Analyst*

And looking in Europe, we were in an environment of a much stronger dollar in the past few years. You had tougher pricing environment there. As a weaker-to-stable dollar help pricing at all over there in terms of market share gain?

Christopher L. Mapes - *Lincoln Electric Holdings, Inc. - Chairman, CEO and President*

No, I really don't think the weaker dollar has played that at all. I would augment Vince's comments earlier that at the end of the day, we're managing the portfolio over there. We do have raw input challenges that our teams are driving into the marketplace. And that is -- that market has its challenges.

And we're going to be aggressive and challenge our teams to continue to recover and expand upon the margin profile that we want to see in that business moving forward.

Operator

This concludes our question-and-answer session. I would like to turn the call back over to Vincent Petrella for closing remarks.

Vincent K. Petrella - *Lincoln Electric Holdings, Inc. - CFO, EVP and Treasurer*

Thank you, Takia, and thank you, everyone, for joining us on the call today and for your continued interest in Lincoln Electric where we're really excited and look forward to discussing our progression of our results in our strategic programs at the end of the first quarter. So thank you very much, and have a good day.

Operator

Ladies and gentlemen, thank you for your participation in today's conference. This concludes today's program. You may now disconnect. Everyone have a great day.
