31-Oct-2024

# Federal Signal Corp. (FSS)

## Q3 2024 Earnings Call


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# MANAGEMENT DISCUSSION SECTION

**Operator**: Greetings and welcome to Federal Signal Corporation's Third Quarter Earnings Conference Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. [Operation Instructions] As a reminder this conference is being recorded.  I would now like to turn the conference over to your host, Felix Boeschen, Vice President Corporate Strategy and Investor Relations. Please go ahead.

## Unverified Participant

Good morning and welcome to Federal Signa's third quarter 2024 conference call. I'm Felix Boeschen, the company's Vice President of Corporate Strategy and Investor Relations. Also with me on the call today is Jennifer Sherman, our President and Chief Executive Officer; and Ian Hudson, our Chief Financial Officer. We will refer to some presentation slides today as well as to the earnings release which we issued this morning. The slides can be followed online by going to our website, federalsignal.com, clicking on the Investor call icon and signing into the webcast.  We've also posted the slide presentation and the earnings release under the Investor (sic) Investors tab on our website.

Before we begin, I'd like to remind you that some of our comments made today may contain forward-looking statements that are subject to the Safe Harbor language found in today's news release and in Federal Signal's filings with the Securities and Exchange Commission. These documents are available on our website. Our presentation also contains some measures that are not in accordance with US generally accepted accounting principles In our earnings release and filings, we reconcile these non-GAAP measures to GAAP measures.

In addition, we will file our Form 10-Q later today. Ian will start today by providing details on our third quarter financial results. Jennifer will then provide her perspective on our performance and update on our internal initiatives and provide an update on our guidance for 2024. After our prepared comments, we will open the line for any questions.

With that, I would now like to turn the call over to Ian.

## Unverified Participant

Thank you, Felix. Our consolidated third quarter financial results are provided in today's earnings release. In summary, we delivered strong financial results for the quarter with 6% year-over-year organic net sales growth, double digit earnings improvement, gross margin expansion and a 200 basis point increase in adjusted EBITDA margin. Consolidated net sales for the quarter were $474 million, an increase of $28 million or 6% compared to last year. All of the growth this quarter was organic.

Consolidated operating income for the quarter was $75.9 million, up $13.4 million or 21% compared to last year. Consolidated adjusted EBITDA for the quarter was $93 million, up $14.5 million or 18% compared to last year. That translates to a margin of 19.6% in Q3 this year, up 200 basis points compared to last year. GAAP diluted EPS for the quarter was $0.87 per share, up $0.16 per share or 23% from last year. On an adjusted basis, EPS for the quarter was $0.88 per share, up $0.17 per share or 24% from last year. Order intake for the quarter was


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again strong with third quarter orders at $426 million, contributing to a backlog of $1.03 billion at the end of the quarter, an increase of $27 million or 3% compared to Q3 last year.

In terms of our group results, ESG's net sales for the quarter were $398 million, an increase of $25 million or 7% compared to last year. ESG's operating income for the quarter was $71.5 million, up $14.3 million or 25% compared to last year. ESG's adjusted EBITDA for the quarter was $87.2 million, up $15.2 million or 21% compared to last year. That translates to an adjusted EBITDA margin of 21.9% in Q3 this year, up 260 basis points compared to last year and performance at the upper end of our current target range. ESG reported total orders of $353 million in Q3 this year, compared to $375 million last year.

SSG's net sales for the quarter were $76 million this year, up $3 million or 4% compared to last year. SSG's operating income for the quarter was $16.8 million, up $3.1 million or 23% from last year. SSG's adjusted EBITDA for the quarter was $17.8 million, up $3.2 million or 22% from last year. That translates to an adjusted EBITDA margin for the quarter of 23.4%, an increase of 350 basis points compared to last year. SSG's orders for the quarter was $73 million, down 3% in comparison to order intake in Q3 last year, which included a $7 million fleet order from a customer in Europe. Corporate operating expenses for the quarter were $12.4 million, compared to $8.4 million last year, with about half of the year over year variance resulting from unfavorable changes in fair value adjustments of post-retirement reserves.

Turning now to the consolidated income statement, where the increase in sales contributed to a $22.7 million improvement in gross profit. Consolidated gross margin for the quarter was 29.6%, up 320 basis points compared to last year. As a percentage of net sales of selling engineering, general and administrative expenses for the quarter were up a 140 basis points from Q3 last year. Other items affecting the quarterly results included a $2.1 million reduction in interest expense associated with a lower average debt levels. Tax expense for the quarter was $18.7 million, up $4.9 million from the prior year, with the increase primarily due to higher pre-tax income levels. Our effective tax rate for the quarter was 25.8% compared to 24.2% last year. At this time, we expect our fourth quarter effective tax rate to be approximately 26%, excluding any discrete items.

On an overall GAAP basis, we therefore earned $0.87 per share in Q3 this year compared to $0.71 per share in Q3 last year. To facilitate earnings comparisons, we typically adjust our GAAP earnings per share for unusual items recorded in the current or prior quarters. In the current year quarter, we made adjustments to GAAP earnings per share to exclude acquisition related expenses. On this basis, our adjusted earnings for the quarter were $0.88 per share, compared with $0.71 per share last year.

Looking now at cash flow, we generated $69 million of cash from operations during the quarter, an increase of $21 million from last year, primarily due to higher net income and working capital improvements. That brings our year-to-date operating cash generation to $141 million, an increase of 55% compared to the first nine months of last year. With the improved cash flow, we paid down approximately $25 million of debt during the quarter, ending the quarter with $158 million of net debt and availability under our credit facility of $557 million. Our current net debt leverage remains low even after taking into account our recently announced acquisition of Standard Equipment.

With our financial position remaining strong, we have significant flexibility to invest in organic growth initiatives, pursue strategic acquisitions and return cash to stockholders through dividends and opportunistic share repurchases. On that note, we paid dividends of $7.3 million during the quarter, reflecting a dividend of $0.12 per share, and we recently announced a similar dividend for the fourth quarter. We also funded $4.4 million of share repurchases during the quarter.


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That concludes my comments and I would now like to turn the call over to Jennifer.

## Unverified Participant

Thank you, Ian. We reported another strong quarter of results which included third quarter records across consolidated net sales, adjusted EPS and adjusted EBITDA margin. Thanks to outstanding contributions from both our groups. Within our Environmental Solutions Group, we delivered 7% year-over-year net sales growth and a 21% increase in adjusted EBITDA with higher production levels, strong demand for our aftermarket offerings and continued price realization representing meaningful year-over-year contributors.

In what is typically a seasonally strong quarter, ESG's adjusted EBITDA margins expanded by 260 basis points year-over-year to approximately 22%, a new quarterly record and the upper end of our current target range. With supply chains normalizing, our teams are laser focused on driving increased throughput across the enterprise and are gaining traction on our build more trucks initiative.

At our two largest manufacturing facilities in Streator and Allegiant, Illinois combined third quarter unit production increased 12% year over year. Positively, we are seeing both supply chain fluidity and quality improve across our ESG segment, which should allow for further production increases and reduce lead times for certain product lines, primarily our sewer cleaners and street sweepers. From a capacity perspective, our access to labor remains good and our large scale capacity expansions that we completed between 2019 and 2022 position us well to profitably absorb incremental volumes into our existing footprint.

Shifting to aftermarkets. Demand for our aftermarket products and services remains strong as revenues grew by approximately 10% year over year. Strength was broad based across our aftermarket portfolio, with rental income service run up for new and used equipment sales all up by more than 10% compared to Q3 of last year, while parts sales were also up 6% year over year. Given the high demand for our equipment and rent to own offerings, our teams are diligently working to optimally balance equipment availability and used equipment sales to best serve our customers' needs.

Additionally, we are growing our parts businesses on numerous fronts, including the further integration of recent acquisitions such as Trackless, our will-fit-parts initiative and increasing parts capture in our existing population base. Importantly, given the essential nature of our products and associated high utilization levels through business cycles, the growth in the aftermarket business has been an important strategic pillar in our efforts to mute cyclicality. In total, aftermarket represented approximately 27% of ESG revenue in the third quarter of 2024.

Our other vehicle based businesses also contributing positively to results with our dump truck body business leading the charge with sales up 18% year over year. The quality of our products industry leading lead times and geographic expansion efforts at our Ox Bodies dump truck business present a unique value proposition that is being recognized in the marketplace.

Shifting to our Safety and security Systems Group, the team delivered another impressive quarter with 4% top line growth, a 22% increase in adjusted EBITDA and a 350 basis point improvement in adjusted EBITDA margin. This improvement was primarily driven by a combination of  volume growth, favorable sales, mix, price realization and efficiency gains. As I will address in more detail later on, we believe our numerous investments over the last decade have structurally strengthened the SSG segment, setting the stage for future profitable growth.


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Lastly, we are particularly pleased with our cash conversion in the quarter, having generated $69 million of cash from operations, representing 120% of net income. On an annual basis, we continue to target 100% cash conversion levels, providing dry powder for organic and inorganic capital deployment opportunities. Shifting now to current market conditions, demand for our products and service offerings remains high, with our third quarter order intake of $426 million representing the second highest third quarter on record. To provide more detail on the composition of orders, domestic publicly funded orders were up 8% year over year, primarily driven by strength in orders for sewer cleaners, which rose 15% compared to prior year. Resilient core funding mechanisms, high equipment utilization, and our ongoing market leadership position continued to drive high demand.

Similarly, demand for our domestic public safety equipment remains at healthy levels, with orders up 12% year over year, driven by robust end market demand and ongoing strategic growth initiatives. Although domestic industrial orders were down 8% year over year, there continue to be strong demand for the majority of our industrial products. In fact, the lower industrial orders in Q3 this year was almost entirely due to a $19 million reduction in orders for our new safe digging products. To be clear, we continue to believe that the adoption of safe digging across North America will prove a meaningful long-term growth driver.

However, given the predominantly industrial contractor base and the fact that safe digging trucks represent one of our more expensive products, it is also one of our most interest rate sensitive new equipment purchases. As such, we have seen customers favor rentals or used equipment purchases to serve their safe digging needs as opposed to buying a new unit. In fact, in Q3 we saw that thesis materialized in our aftermarket business in the form of double digit increases in our combined safe digging rental income and used equipment sales. As one of the largest manufacturers of hydro excavation trucks in North America, we believe our multipronged approach between new, used, rental and rent own availability offers our customer base important flexibility in accessing equipment. We also believe it sets the foundation for Federal Signal to capitalize on this multi-year adoption tailwind while decreasing the cyclicality of our safe digging business.

In fact, approximately 80% of our sewer cleaners are now equipped with hydro excavation packages, and we continue to see strong customer demand for these multi-use products. We believe this enables another avenue for Federal Signal to capitalize on the rising adoption of safe digging across North America.

Excluding safe digging, our other domestic industrial orders increased 4% year over year. Dump truck body orders rose 13% year-over-year, driven in part by ongoing execution on our strategic growth initiatives and high demand for public road construction equipment. With approximately $100 billion of the $840 billion of funds authorized under the Bipartisan Infrastructure Law spent to date, our teams continue to strategically position our businesses to capitalize on what we see as rising demand in the form of greater parts consumption and equipment sales opportunities and other aftermarket services over a multi-year period.

One such example is our road marking and line removal services businesses with HighMark which in conjunction with MRL Blasters, continues to enjoy strong demand for our suite of road marking and stripe line removal product and services. In summary, demand for our product remains high. Our teams are focused on executing on our growth initiatives and building more trucks while maintaining a healthy order intake.

I now want to provide an update on a number of internal initiatives that support our through the cycle target of double digit top line growth. Recall that these targets are consistent with our actual track record at a 14% revenue CAGR since 2016. Similar to our actual experience over that timeframe, we expect a fairly even contribution over the long term between organic and inorganic growth as part of these targets.


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First, we are pleased to announce that we closed the acquisition of Standard Equipment earlier this month. Similar to other acquisitions in this arena, the addition of Standard further builds upon our aftermarket growth strategy that was originally put into action in 2016 as we expand our parts services and rent to own offerings. From a strategic perspective, our growing aftermarket ecosystem allows us to better serve our customer needs throughout the entire business cycle while targeting historically underpenetrated cohorts of Federal Signal customers and muting cyclicality. We believe the addition of Standard further accelerates those efforts with integration efforts already well underway.

More broadly, our M&A pipeline remains active with numerous opportunities currently under evaluation spanning new OEM equipment adjacencies within our ESG and SSG segments, further aftermarket growth opportunities and strategic asset within verticals that we already operate in.

Second, we are identifying new opportunities to harness the power of our growing specialty vehicle platform, which we ultimately believe will yield incremental market share and margin expansion runway. One such initiative is the optimization of our go-to-market strategy, which has been critical to the sales growth of the products that we manufacture. We go to market through three primary channels, resulting in a balanced distribution mix between direct, tthird party distributors and exclusive dealers. Although it can vary, for context, last year, our direct channel represented approximately 40% of our net sales, whereas the remaining 60% of our net sales was fairly evenly split between third party distributors and our exclusive dealer network.

Within each of these channels, we are actively looking to optimize cross-selling opportunities and other distribution synergies that allow us to best serve our customers. As an example, within our direct channel, our combined metal extraction support platform of Ground Force & TowHaul has grown net sales by more than 60% since the purchase of TowHaul in 2022, while expanding margins. This growth was primarily achieved through the identification of certain distribution synergies, a targeted effort to increase aftermarket revenue capture, material cost reductions, and other cross-selling opportunities.

In fact, this quarter, Ground Force & TawHaul hosted our first joint booth at MINExpo Trade Show in Las Vegas and received excellent customer feedback. We're also growing through our valued third party dealers and distributors. Great examples of this are our Ox Bodies and Travis businesses, which produced dump truck bodies and specialty dump trailers. In both instances, our teams have been actively expanding our geographic reach with the addition of new third party dealers and distributors. Ox Bodies specifically continues to make strides in expanding into key strategic geographies such as Texas Florida.

Our exclusive dealer channel, primarily serves certain municipal product lines, including sewer cleaners and street sweepers. Many of our dealers have been valued partners for decades and consequently have intimate knowledge of our products, strong relationships with end users, and provide outstanding service to our customers. As a reminder, this exclusive dealer network is comprised of a combination of private, family owned businesses and private equity backed operations, as certain dealers have worked through natural succession planning, we have been proactively addressing areas of share opportunity in conjunction with our dealer partners and our direct team. As part of that process, in recent years, some of our existing high performing dealers have assumed the right to sell our products in certain states, while in other situations, our direct team has assumed certain US territories, including the Carolinas, which our direct team assumed in June of 2020 for an initial investment of approximately $6 million.

Four years into assuming the Carolinas Territory, the team has grown combined sales of new sewer cleaners and street sweepers by more than 80%. The team is now working on opportunities to sell incremental federal signal products like trackless and dump truck parts. With its strong performance in the Carolinas, this team has also


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expanded into neighboring Virginia as part of a recent dealer transition. I would also like to thank this team for their efforts to deliver critical supplies to citizens of North Carolina impacted by Hurricane Helen.

Looking ahead, while we believe we are in the later innings of large scale territory assumptions, we continue to see runway for further share expansion through go to market optimization as we capitalize on our growing specialty vehicle platform.

Lastly, we have structurally strengthened our Safety and Security Systems Group over the past two years, setting a renewed foundation for the next leg of profitable growth. As many of you know, Federal Signal's origin dates back to the SSG segment, which has undergone a slew of transformations history over 120 years. Since 2016, our focus is centered around a couple of critical aspects, including a rigorous 80/20 approach and reinvigoration of new product development efforts. These efforts have not only translated to higher sales and improved customer service, but SSG's EBITDA margins have also expanded by more than 800 basis points compared to 2016.

Additionally, we have invested in capacity with the purchase of our production facility in University Park, Illinois in 2022 and with the addition of several printed circuit board lines as part of our in-sourcing efforts. These investments have expanded available capacity, increased internal efficiencies, and reduced our reliance on Asian suppliers. In fact, across all of Federal Signal, less than 5% of our direct material purchases come from outside North America. With ample capacity at the University Park facility, we believe we are well-positioned to profitably grow within our footprint in coming years. As we approach the next phase of growth at SSG, we will look to build upon this strengthened formation in the form of both organic market share and inorganic growth opportunities.

At this time, we are also formally raising our SSG EBITDA margin targets to a range of 18% to 24% from 17% to 21%. Consistent with our prior approach to margin targets, these targets are meant to be annual and through the cycle targets. Internally, these targets present the guideposts through which we intend to operate and we have also aligned our compensation practices with margin targets.

Turning now to our outlook for the rest of the year. Demand for our products and our aftermarket offerings remains high with our order intake this quarter, contributing to a backlog which provides us with excellent visibility well into 2025. With our third quarter performance, our current backlog and continued execution against our strategic initiatives, we are raising our full year adjusted EPS outlook to a new range of $3.30 to $3.40 from the prior range of $3.20 to $3.35. We are also narrowing our full year net sales outlook to a new range of $1.86 billion to $1.88 billion from the previous range of between $1.85 billion and $1.9 billion.

Our updated net sales outlook takes into account the normalizing chassis procurement patterns that we have previously discussed, which is resulting in lower chassis parts pass through revenue year over year. While the impact to EBITDA is immaterial, we expect that fewer chassis sales will represent a full year over year net sales headwind of approximately $20 million, with over half of that headwind expected in the fourth quarter. This outlook reflects our view of continued healthy demand for our new equipment parts and aftermarket services.

Lastly, we are maintaining our CapEx outlook of $35 million to $40 million for the year.

At this time, I think we are ready for questions. Operator.?


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# QUESTION AND ANSWER SECTION

**Operator**: Thank you. At this time, we'll be conducting a question-and-answer session. [Operator Instructions] One moment please while we poll for questions. Our first question today comes from Mike Shlisky of D.A. Davidson. Please proceed with your question.

A

Good morning, Mike.

Q

Good morning, Jennifer. Thanks for taking my questions, everybody. I didn't hear much comment on your rental fleet, your vacuum trucks and other assets that you grew out for rent. Can you maybe update us on how that's been going? And have the recent storms been a tailwind for that business? You said that the assets in those affected regions and maybe a little bit about your plan to invest in going forward?

A

Yeah. Mike, I think it was part of the strength of the aftermarket business that we saw during the quarter. I think overall aftermarket revenues were up 10% year over year. That really was driven by growth that we saw in really all four components of our aftermarket revenue streams. That that would be parts, rental income, used equipment sales and service. Specifically on rental income, rental income was up 12% year over year. A lot of that was driven by the demand that we're seeing for rentals of safe digging. Used equipment sales also, they were up 15% year over year. Again, safety was a piece there. And I think we made reference in our comments to a current -- the customers are favoring right now given the higher interest rate environment and given the safe digging trucks, new trucks are one of our higher price point items. I think there is currently a preference to rent or to buy use. And certainly that's what we saw during the quarter with the strength of the aftermarket business.

Q

Okay. All right. Just kind of moving on here. Class 8 vocational truck demand. That seems to be up quite a bit as well. From an industry perspective, the first order for 2025, they're coming in. It seems to be really close to all time record numbers. I guess. I guess first of all, it feels, you know, participating in any of that. Are you are you pre-buying any chassis in advance of emissions changeovers in 2027 already at this point? Or just do you see some giant blockbuster year ahead? Or are all your customer order patterns and your order patterns really more normal and in line with the demand you see for 2025? And perhaps it's just somebody else is placing these very large early, early orders here. Just any kind of comments on whether you're looking to secure Class 8 chassis way in advance, given what's going on in the market here?

A


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I'll start with, you know, demand for our product remains high. We talked about our public funded product, which include, you know, our Class 8 sewer cleaners was up in Q3, 8%. Sewer cleaners specifically were up 15%. Dump truck bodies were up 13%. So in -- we've talked about kind of the normalization of chassis buying patterns. And so we typically, you know, purchase about 50% of those chassis. And, you know, we are in the -- right now, we are purchasing chassis for next year. With respect to the 2027, the chassis aren't available at this particular point. But, you know, could we see, you know, pre-buying based on past patterns? Yes. And we are currently working closely. We have a team that's led by Mark Weber that's working closely with the OEM and the chassis partners in anticipation of these regulation changes. So we feel like we're very well positioned as we move forward.

Q

Okay. Maybe one last one for me. There's all this talk about of SSG margin expectations coming upward in the -- in this quarter's guidance, but it was actually ESG that actually hit an all time record for margins in the quarter. Is there anything seasonal or anything you see in the pipeline that would suggest that in the fourth quarter there's a step sequentially downward in ESG margins, or is where you're seeing last few quarters kind of a great baseline here?

A

Yeah. I think, Mike, some of it goes back to the strength that we saw in the aftermarket business during the quarter. A lot of the projects take place during the summer months when the weather is nicer in certainly the northern parts of the US and up in Canada, which is a really important market for us. So as the weather starts to kind of deteriorate, you know, later into the fourth quarter and into Q1, that business which tends to have a slightly more attractive margin profile, that tends to slow down a little bit. But as we sit here today, you know, yesterday the weather was in the 80s in Chicago. So, you know, hopefully that will continue further into Q4.

Q

Okay. Thanks for the color. I'll leave it there. Thank you so much.

A

Thank you.

**Operator**: <Q>: The next question is from Jacob Moore of KeyBanc Capital Market. Please proceed with your question.

A

Good morning, Jacob.

Q


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Hi. Good morning. I'm on for Steve Barger today. Thanks for taking our questions. First for me, Jennifer, thanks for the color on the industrial versus municipal order trends. If I could dig in a little bit. Can you help us understand what's in the current backlog from those customers where demand is weak versus the rest of the backlog? Has there been any shifts in the backlog for what's already been ordered? And how long do you think this current order trend could run for?

A

I don't know that we've seen any dramatic shifts necessarily in the municipal backlog. Obviously, we talked about the lead times for sewer cleaners and street sweepers being, you know, longer than we'd like, quite frankly. Those are both municipal products. We haven't really seen a shift -- with the extent of that backlog, it gives us really good visibility for those product lines into 2025 and even into the early part of 2026. So I don't think we've seen much of a change. We did -- we have talked a little bit about a shift in the mix of the chassis provided by us or versus provided by the customers. And I think we mentioned in our prepared remarks that can have some impact on our year over year comparisons, both on orders as well as revenue. So that's probably the one thing is as we think about a change in kind of what's in the backlog, I would say the mix of chassis is probably the biggest change.

A

And I guess I would add there that, you know, with the exception of the shift from purchasing new hydro excavation equipment to customers now renting and buying used equipment, you know, which we believe is, you know, a critical part of our strategy in terms of muting cyclicality. We were pleased with orders as we move forward, and it gives us really good visibility into 2025 and even into 2026 in terms of the strength of the demand for our products.

Q

Okay. Got it. That's helpful. Thank you. Second from me, you've posted really impressive incremental margins this year, 48% this quarter averaged 44% for the year. Is it mix that's driving that or do you have better price in the backlog that you're producing? And secondly, to that, should be thinking that you can maintain this structurally higher level of incremental margin going forward?

A

Yeah, I think mix was a piece. Again, we talked about the aftermarket mix. And I think, you know, that was that's obviously a slightly higher margin profile. So that was a component. We saw some normalization of material cost on the SSG side and that was a factor of the margin improvement. But I think if you look at the you know, the leverage we had in this quarter, it was probably higher than what we would typically expect over the long term. And I think over the long term, if you go back and look at, you know, how we've progressed really since 2016, it's really been in the incrementals have been north of 20%. Again, there is some seasonality to the business during during Q3 with the strength of the aftermarket business. Remember, we've also added a lot of capacity in the last couple of years. So as we grow into that, we think that's where there is some potential from a margin standpoint as we go forward.


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Q

That's helpful. Thanks. And then maybe I'll ask related one to that answer. I know you're not guiding to 2025 yet, but given those capacity expansions you just mentioned and your backlog visibility, can we think about the average of the last three quarters this year as the baseline from which you'll grow in 2025? Or are there any reasons that you'd be running revenues lower than the $485 million to $490 million range?

A

Yeah. I think, again, if you think about the averaging that there is seasonality and if you look at the last couple of quarters, Q2 and Q3 tend to be, you know, higher because of that strength of the aftermarket business. But, you know, we're -- we have a goal internally. It's called build more trucks. And so our primary objective is to increase production while maintaining that healthy order intake to really reduce lead times. And as we as we go into 2025, given where the backlogs are, I think that's going to continue to be our objective. We've made some great progress. I think those -- the two primary manufacturing facilities on the ESG side. We talked about a 12% production increase year over year. So we are seeing the benefits of that initiative. We haven't necessarily made much progress to reduce lead times, as we would have hoped, and that but that's primarily because orders have been coming in. I mean, for the first nine months of this year, our book-to-bill is still in excess of one, and that's with some pretty significant headwinds. We talked about the $17 million year-to-date chassis headwind. There's about a $17 million headwind from two large fleet orders we had on the SSG side. And there's also an $8 million headwind from last year's orders, including trackless. So if you think about all of those things, increasing production while maintaining healthy orders, that's really what our objective is and that will continue as we go into 2025.

A

And just, you know, looking at our backlog is up 3% year over year. It does, as I mentioned earlier, give us good visibility into 2024, beginning of 2025 and even into the beginning of 2026.

Q

Okay, got it. That's all very helpful. Thank you for taking the questions.

A

Thank you, Jacob.

**Operator**: The next question is from Ross Sparenblek of William Blair. Please proceed with your question.

A

Good morning, Ross.


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Q

Good morning, Jennifer. This is Sam Karlov on for Ross. Thanks for taking my question. I just wanted to get some color on -- or I appreciate the color on lead times. I was wondering if you could just give us some color on what the remaining hurdles are to kind of get those lead times down, whether those are kind of internal or external?

A

Yeah, I would say a couple of critical things. One is, you know, continued supply chain is much better today than it was a year ago. But we need that supply chain to continue. As we talked about, for example, in Q1, we had a quality issue with one of our suppliers. We worked through that. So we need not only to get the parts. We need quality parts. Number two is we have a number of internal initiatives, particularly at Vactor and Elgin because I think we've done a pretty good job at majority of the rest of our businesses, you know, where we have both maintained high demand and reduced lead times. But because our orders have continued to be strong, despite the fact that production at Elgin and Vactor was up Q3 12%, we are very focused on increasing building more trucks. We've engaged a third party at Elgin. We talked about it as part of our Federal Signal operating model. We're in the middle of that process and we are laser focused on increasing production while maintaining a healthy order intake.

Q

Got it. That's super helpful. And then kind of switching over to Standard Equipment. Did you guys give or kind of quantify what the revenue of that acquisition would look like?

A

No, because just to give you some color, Sam. So Standard, for the last couple of years, Standard revenues have run in the $40 million to $50 million range. The majority of that is from Federal Signal municipal products. As we are -- we're working through integration with the Aftermarket's team, we're going to apply our 80/20 model so that could be changes to the revenue dynamics there. Obviously, we sold units to Standard Equipment as a manufacturer. So there will be some kind of balance there. But we expect the incremental revenue contribution in 2025 to be in the range of about $20 million. And we expect that to build over time, particularly as we look to grow that Aftermarkets business, but -- and also then push additional Federal Signal products through that channel. But overall, you know, we expect acquisition to be accretive to both earnings as well as cash flow in 2025.

Q

Got it. That makes a lot of sense. And so, I mean, seasonally, should we think about you said $20 million to $25 million 2025. So about $5 million in the fourth quarter or is there some seasonal variation there?

A


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There's some seasonal variation. Again, you know, I think it's somewhat weather impacted because that primarily in in Illinois and Indiana. So with weather and we had an impact primarily in Q4 and in Q1. There's typically some seasonality with Q2 and Q3 geeting -- typically getting stronger.

Q

Got it. And then that $20 million revenue benefit, should we -- how should we think about the split between aftermarket new equipment, how that flows through?

A

Yeah, it's roughly 50/50. I mean, they do a really nice job on the parts side of the business as well as service. They -- so it's a fairly even split between between the two.

Q

Got it. That's super helpful. I will leave it there.

A

Thanks, Sam.

A

Thanks, Sam.

**Operator**: The next question is from Chris Moore of CJS Securities. Please proceed with your question.

A

Good morning, Chris.

Q

Hey, good morning, guys. Good morning. Right. Yeah. Maybe we'll stay with aftermarket for a moment. So obviously, lots of companies talk about aftermarket sales. One thing, Jennifer, that you've referenced a few times is this kind of growing ecosystem within Federal Signal that that kind of positions you uniquely. I just wonder if maybe you could go into that a little bit deeper.

A

Yeah, absolutely. So we think of -- it's important to look at kind of all of the revenue streams of aftermarket, the revenue, the rental, the service, the parts and the used equipment. And, you know, the hydro example is a good


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one. Interest rates are higher. And so we've seen a shift in terms of customers, you know, are having more challenging time affording new equipment that, you know, hydro equipment is our most expensive equipment that we sell. So they will favor rentals or  used equipment. As we go forward, I think what's also really unique about Federal Signal and Aftermarkets is our ability to kind of leverage and optimize that ecosystem. So, as we acquire new companies like Trackless, we have the existing bricks and mortar and distribution channel to increase the sales of their new equipment, of their parts, of their service and their used equipment. Think about it. The same people that buy municipal street sweepers are also buying Trackless equipment.  So it is what is unique and I think will give us an advantage going forward because we're going to continue to organically grow and introduce new products that we can push through that aftermarket ecosystem. And as we acquire companies, we'll be able to leverage that ecosystem.

And at the end of the day, we're looking at how do we best serve our customers, how do we have that stickiness with customers? And we tried -- on the call, on the prepared remarks, we gave some specific examples of successes that we've had leveraging this ecosystem. And again, I'd reiterate, it really is what distinguishes Federal Signal is the ability that we have this ecosystem and we have common end customers for many of our products.

A

And Chris, I'll just kind of give some data points on kind of the growth that we've see in the aftermarket business really between 2018 and 2023. If you look at our parts sales, it's grown 83% and our rental revenue has grown by about 32%. So that just gives you an indication of kind of the traction that we've been getting on this initiative.

Q

Got it. Very helpful. And since from 2018 to 2023, from a kind of geographic penetration, looks much different.

A

Yeah, absolutely.

A

Absolutely.

A

Yeah.

A

And again, as we talked about, it's mute cyclicality of earnings streams. So again, that hydro excavation example. If they can't afford new equipment and we've got rental and used equipment either through us or our valued dealer partners.


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Q

Got it. Very helpful. Switch gears. So order cancellations can be, you know, kind of a helpful sign in judging demand and lead times. Just trying to get a sense of what you're seeing on that front.

A

Yeah, we haven't really seen anything significant, Chris, to date. It's typically not something in our history that we've seen. In our businesses, a lot of times on the municipal side of the business, it's part of a public bid situation. So that's typically not been something we've seen much of.

Q

Got it. And maybe the last one for me, I mean, we talked about this a few quarters ago. Cost looks to be, you know, the biggest hurdle for a significant move, and customers going towards electrification. Just curious kind of what you're seeing on the EV side these days.

A

Sure. So, as you know, we've got our EV street sweeper products, EV dump truck products. We've done -- the tteams have done a nice job. They've got a good working prototype with respect to our Trackless products. We saw a large order that started in Q2 of seven piece of equipment at a New York and continued into Q3 for our EV street sweeper product. So, you know, we'll continue to demonstrate that product. We get very positive feedback from the field. The question often is affordability. But we believe as we move forward, this is an important product offering for our customers.

Q

Fair enough. I will leave it there. Thanks, guys.

A

Thanks, Chris.

**Operator**: The next question is from Greg Burns of Sidoti and Company. Please proceed with your question.

Q

Good morning, Greg.

A


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Good morning. Just staying on the the aftermarket. Given the strong demand for rental, are you constrained in any way on that side of the business? Is there need to maybe invest more into your own fleet of vehicles? And how do you balance that maybe against the need to kind of reduce lead times and like you said, build more trucks?

A

Yeah. I think, Greg, we -- it's obviously something we monitor closely and we can -- we monitor utilization levels before making decisions about whether to add to the fleet. We talked earlier in the year about an incremental investment of about $20 million going into the fleet for used and rental. That is -- that at the time that was going to be second half, second half weighted. And so I think you saw some of that during Q3 and that will likely continue into Q4. So we are using production at our facilities, but we don't necessarily get the revenue or the income immediately on those that comes up more over time. And so I think with where we sit today, I think that that we feel comfortable at that level particularly as you think about the strength of the used equipment. So as we saw used equipment, sales were up 15% year over year in the quarter. That creates a need obviously to then replenish so the fleet size remains the same. But as we -- I think for the -- for this year, for 2024, I think we're in good shape. And as we head into the planning process for 2025, that's where we'll make make decisions about what, how much we need to add to the fleet. But again, our our approach really is a multipronged approach where we rely on several valuable valued rental partners on the rental side of the business as well.

Q

Okay. And then did you have any production disruptions from the hurricane, the hurricane season? And then also, I was just wondering if there's been any change in demand patterns because of the election or maybe any uncertainty going into the back half of the year. Have you seen any kind of pause in the business?

A

Yeah. I'll start with the hurricane. We had our service center in Tampa was down for a couple of days, but the teams did a nice job in terms of getting back up and running. Again, our teams in the Carolinas just did a fantastic job assisting and aiding many citizens and delivering supplies in North Carolina. With respect to going forward, to date, we haven't seen any impact regarding the election. We did -- there's a lot of discussion around tariffs. We called out in our prepared remarks that, you know, less than 5% of our direct purchases are outside of North America. So we think we're well positioned regardless of who wins the election. And we often get asked about kind of infrastructure spending. To date it has had minimal impact. We still remain in a strong order patterns. It was bipartisan support for that piece of legislation. So as we move forward, we feel pretty good.

Q

All right. Thank you.

**Operator**: The next question is from Dave Storms of Stonegate. Please proceed with your question.

Q


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Good morning.

A

Good morning, David.

Q

Good morning. Just wanted to start with the strong cash position. Are there any growth initiatives that may have been outside of your plans or scope at the beginning of the year that maybe become more feasible given the strong cash growth on the year?

A

Yeah. I think, Dave, we -- I think we went into the year with a CapEx range of about $35 million to $40 million, and we still think that's appropriate. As we go into 2025, there are probably, with each of our businesses, could present their request with the capital and the different organic initiatives that they might need some funding. So we'll take a look at that as we we go through our planning purposes. Again, that $35 million to $40 million, about half of that -- half CapEx of maintenance CapEx and half is growth. Organic investments continue to be a priority for the use of our capital. So we want to keep investing in those businesses. But I would say there hasn't necessarily been a change in our priorities or in the projects that we want to invest in during this year. But as we go into 2025, it's something we'll take a look at, just depending on the businesses and depending on the strategic initiative.

Q

Understood. Very helpful. Thank you. And then just one more. How do you feel about your current capacity levels between labor and square footage of processing lines and maybe how that fits with the current burn rate of your backlog?

A

So, between the period of 2019 and 2022, we added significant capacity. We made $25 million investment at our facility in Streator, but we also made a number of other investments. We purchased the Elgin facility. We purchased University Park facility, and we highlighted some of the benefits of that in our prepared remarks. But we also made capacity expansions at Rugby, Lake Crystal for our dump truck businesses. So we believe right now that we have sufficient capacity to support us going forward.

I'd also highlight that with respect to our CapEx, that growth CapEx, a lot of it's been focused on efficiencies and how do we build more trucks and we've had good success there. So as we move forward, we're very well positioned to be able to leverage the capacity investments that we've made, both in terms of additional space and the equipment investments that we've made to increase our production.


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That's very helpful. Thanks for taking my questions and good luck in fourth quarter.

Thank you.

**Operator**: There are no additional questions at this time. I'll now turn the conference back over to Jennifer L. Sherman for closing remarks.

## Unverified Participant

Thank you. In closing, as we enter this Thanksgiving season, I want to spend a moment to thank our dedicated employees and loyal customers and our dealers and distributors. Thank you for joining us today and we'll talk to you soon. Bye, bye.

**Operator**: This concludes today's conference. You may disconnect your lines at this time. Thank you for your participation.

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