PARTICIPANTS

Corporate Participants

Lou Anne J. Nabhan – Investor Relations Contact, Hamilton Beach Brands Holding Co.
Gregory H. Trepp – President and Chief Executive Officer, Hamilton Beach Brands Holding Co.
James H. Taylor – Vice President, Chief Financial Officer and Treasurer, Hamilton Beach Brands Holding Co.
R. Scott Tidey – Senior Vice President-North America Sales and Marketing, Hamilton Beach Brands, Inc., Hamilton Beach Brands Inc.

Other Participants

Peter S. Benedict – Analyst, Robert W. Baird & Co., Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Good morning. My name is Tiffany and I will be your conference operator today. At this time, I would like to welcome everyone to the Hamilton Beach Brands Holding Q1 2018 Earnings Conference Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions] Thank you.

Lou Anne Nabhan, Investor Relations Consultant for Hamilton Beach Brands Holding Company, you may begin your conference.

Lou Anne J Nabhan, Investor Relations Contact, Hamilton Beach Brands Holding Co.

Thank you, Tiffany. Good morning, everyone. Welcome to the first quarter 2018 earnings conference call and webcast for Hamilton Beach Brands Holding Company.

Greg Trepp, President and Chief Executive Officer; and Jim Taylor, Vice President, Chief Financial Officer and Treasurer will discuss the company's first quarter results. Also participating in the Q&A will be Al Rankin, Executive Chairman of Hamilton Beach Brands Holding Company; and Scott Tidey, Senior Vice President-North America Sales and Marketing for Hamilton Beach Brands.

Yesterday, after the market closed, the company issued an earnings release announcing the first quarter 2018 results and filed a 10-Q with the SEC. Both documents can be found on the company's website at www.hamiltonbeachbrands.com. This afternoon a replay of today's call will be posted on the website and, when available, a transcript will be posted.

Today's presentation contains forward-looking statements which are subject to risks and uncertainties that could cause actual results to differ materially from those expressed in either the prepared remarks or during the Q&A.

Additional information regarding these risks and uncertainties was included in our earnings release and 10-Q. The company disclaims any obligation to update these forward-looking statements which may not be updated until our next quarterly conference call, if at all. Also, certain amounts discussed during today's call are considered non-GAAP. The non-GAAP reconciliations of these amounts are included in our earnings release.

And now, I'll turn the call over to Greg.

Gregory H. Trepp, President and Chief Executive Officer, Hamilton Beach Brands Holding Co.

Thank you, Lou Anne. Good morning, everyone and thanks for joining our call. My remarks will cover the first quarter performance of our two business segments, Hamilton Beach Brands and Kitchen Collection.

Hamilton Beach delivered a strong performance in the first quarter. Revenues increased to $11.3 million or nearly 10% versus last year. The revenue growth was primarily driven by the international and U.S. consumer markets and was mainly the result of increased sales of higher priced products. The higher revenues also reflect favorable foreign currency movements, particularly in Mexico and Canada.

We're very pleased that we are experiencing growth across all of our businesses due in large part to continued progress with our Strategic Initiatives, and we believe we should see positive momentum going forward. Also important to note, we had a slow start to the year last year, so our comp period was a little low. Based on customer decisions we have confirmed, we do not project the growth to continue at the same percentage rate, but we do expect continued growth. As customer decisions become confirmed, we will have more clarity on our full-year projection.

Operating profit for Hamilton Beach was $4 million in the first quarter, a $3.2 million increase from last year. The increase primarily reflects higher gross profit this year partly offset by a $1.9 million increase in SG&A expenses, mainly from higher employee-related costs. The improved operating performance, as well as benefits from a lower effective income tax rate, resulted in net income for Hamilton Beach increasing to $2.8 million this year compared with $689,000 last year.

As I mentioned earlier, we are pleased with the growth we delivered. More importantly, we delivered meaningful progress on all of our initiatives. As examples of this, I would highlight that we delivered growth in our higher-end products in the first quarter, including our Hamilton Beach FlexBrew line and our Weston bag sealer line, as well as a variety of products in our Wolf Gourmet and CHI brands.

Our commercial business grew driven by increased demand of existing and new products such as our high performance blender line which continues to grow globally. Our international business increased across a number of markets. And after a strong performance in e-commerce channel in 2017, we expect that to continue throughout 2018.

And lastly, a number of our introductions into new categories are coming to market in the first half of this year, which we expect will generate incremental revenue in the years ahead. We have a new line of Commercial Chamber Sealers that have just been introduced. We also have products coming to market in our Laundry segment and the Coffee Serving segment, among others.

We will continue to focus on strengthening the consumer market position of our various product lines by introducing new innovative products, as well as upgrades to certain existing products such as the newest generation of our Hamilton Beach FlexBrew coffeemaker product that I mentioned, as well as through promotions, increased placements and branding programs.

We also recently introduced a Wolf Gourmet Multi-function Cooker and Wolf Gourmet Precision Griddle that we expect will help to generate incremental revenue growth. We expect our growing global commercial business to benefit from broader distribution of several newer products, including our new Quantum high-performance commercial blender and the Otto Juice Extractor.

Next, turning to our Kitchen Collection business. In the first quarter of 2018, we continued to face headwinds from declining foot traffic in our stores, despite progress made by the team on several fronts. The team continues to deliver strong gross margins, control inventory levels and reduce

SG&A expenses. Delivering on all these important aspects of the business is very challenging when the comparable store sales were down, but the Kitchen Collection team has done a solid job in that environment. During the first quarter, we closed 11 stores. However, the higher-than-expected drop in comp sales was difficult to overcome.

Kitchen Collection revenues decreased $4.6 million in this year's first quarter, primarily because of the decline in comparable store sales and a loss of sales from the closure of underperforming stores. The decrease in comparable store sales can be mainly attributed to the decline in customer traffic and a shift to lower priced products, which resulted in a reduction in store transactions and a decrease in our average sales transaction value.

Kitchen Collection's operating loss increased $1 million this year compared with the first quarter of 2017, primarily because of the decline in sales of comparable stores.

Given this very challenging market environment, Kitchen Collection continues to focus on optimizing its store count for current foot traffic trends. We continue to focus on building flexibility into our store portfolio by moving all leases to one year or less over time. We expect to have 70% of our leases at that goal by the end of 2018. We will right-size our store portfolio and cost structure based on profit targets outlined store-by-store. If we cannot make an acceptable return, we will close the store. If Kitchen Collection cannot reach acceptable terms with its landlords as leases come up for renewal, the pace of store closings could increase.

With that overview of our two segments, let me turn the call over to Jim for additional details regarding our first quarter financial results.

James H. Taylor, Vice President, Chief Financial Officer and Treasurer, Hamilton Beach Brands Holding Co.

Thanks, Greg, and good morning, everyone. As we reported, our consolidated revenues increased 4.5% to $146.6 million in this year's first quarter reflecting the strong revenue growth at Hamilton Beach, partially offset by the lower revenues at Kitchen Collection.

We reported a consolidated net loss for the 2018 first quarter of $418,000 or $0.03 per share, compared with a consolidated net loss of $1.4 million or $0.10 per share last year. The current quarter results reflect the strong revenue and operating profit performance at Hamilton Beach partly offset by lower operating results at Kitchen Collection.

Our consolidated effective income tax rate in the first quarter was 25.9%, compared with 37.5% in last year's first quarter, and we expect our full year 2018 rate to be in the range of 26% to 28%.

Our consolidated EBITDA for the first quarter of 2018 was $1.2 million.

As of March 31, 2018, we had consolidated cash on hand of $2.4 million, compared to $10.9 million as of December 31, 2017 and $5.6 million as of March 31, 2017.

Also as of March 31, 2018, our consolidated debt was $85.5 million, compared to $51.3 million as of December 31, 2017, and $59 million as of March 31, 2017. Our debt increased primarily because of a planned increase in our inventory levels to support higher sales forecasts in the first half of 2018.

Now, let me discuss the outlook for our two business segments.

At Hamilton Beach, we expect revenues to increase moderately in 2018 compared to 2017. While we are pleased with the growth we delivered in the first quarter, as Greg indicated, based on what we know about the balance of the year, we do not anticipate revenue growth to continue at that same percentage rate that we experienced in Q1.

Our revenue outlook reflects modest growth in the consumer retail market and moderate growth in our international commercial markets. Additionally, we expect new or enhanced product introductions and an increase in higher priced, higher margin product placements resulting from the execution of our Strategic Initiatives to help drive the revenue growth.

Product demand is expected to continue to increase in the second quarter over 2017 levels based on current customer commitments. Firmer commitments for the second half of the year and the holiday selling season are expected to occur in the second and third quarters. As a result, we continue to expect moderate revenue growth at Hamilton Beach in the first half of 2018 with modest growth in the second half of the year. But as we gain better visibility, we could revise our expectations.

Benefits of increased revenues are expected to be partly offset by product cost inflation, which we aim to mitigate by adjusting product placements and product pricing as market conditions permit, as well as increased cost to implement Hamilton Beach Strategic Initiatives. We expect 2018 operating profit for Hamilton Beach to increase moderately compared to 2017. We will continue to closely monitor commodity and other input costs as well as currency effects.

Net income is expected to increase substantially over 2017 because of a lower effective corporate income tax rate, as well as the absence of the provisional charge that we recorded in 2017 for the U.S. Tax Reform Legislation.

We expect full-year 2018 cash flow before financing activities to be higher than 2017.

Our capital expenditures in the first quarter were $2.3 million, and we estimate an additional $8.3 million for the remainder of 2018. These planned capital expenditures are primarily for improvements to our information, technology infrastructure, tooling for new products, and distribution warehouse improvements.

Now turning to Kitchen Collection, the full-year 2018 revenues are expected to decrease moderately compared to 2017, reflecting the ongoing headwinds Greg described, as well as the first quarter 2018 store closings. Kitchen Collection plans to continue to focus on maintaining strong gross margin, controlling operating expenses, and optimizing working capital. However, without an increase in store traffic, we expect Kitchen Collection's 2018 operating and net losses will be higher than in 2017.

At Kitchen Collection, we expect cash flow before financing activities to result in the use of cash in 2018.

Kitchen Collection's capital expenditures are expected to be approximately $500,000 in 2018, of which $100,000 was expended in the first quarter.

We believe Kitchen Collection's focus on the customers' experience in combination with improved product offerings, a focus on sales of higher margin products, merchandise mix and displays, closure of underperforming stores and optimizing its expense structure, should contribute to improvements in operating results over time.

Our consolidated full year 2018 net income is expected to increase substantially over 2017, driven by a lower effective tax rate and improved operating results at Hamilton Beach.

This concludes our prepared remarks. I'll now turn the line back to the operator for Q&A.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Your first question comes from the line of Peter Benedict with Baird. Your line is open.

<Q – Pete Benedict – Robert W. Baird & Co., Inc.>: Hey guys. How you doing? Good results here. I wanted to start out just within the Hamilton Beach segment the revenue performance. How did that compare to your internal expectations 90 days ago, any particular lines or channels that were notably better than what you expected?

<A – Greg Trepp – Hamilton Beach Brands Holding Co.>: This is Greg, Peter. I think we had a forecast for this level maybe a little higher . . . but we really ended up having a nice growth really across every division in every market. So, I think it was a little better than we thought the first quarter could have been and probably a little short of the high end of the range we looked at. So we're somewhere in the middle.

<Q – Pete Benedict – Robert W. Baird & Co., Inc.>: Okay, good. Maybe a little bit on how the business is playing out, kind of, online versus brick-and-mortar. Can you give us a sense for what the e-commerce penetration was in the quarter and again, was there any notable traction or trajectory change in terms of your growth online in the quarter versus brick-and-mortar versus how those had been running, let's say, last year.

<A – Scott Tidey – Hamilton Beach Brands Inc.>: This is Scott, Peter. So, looking at specifically in the U.S. consumer market. I think we continue to see the same trends we've been seeing mostly through 2017 where currently more products are being consumed through the online channels. We continue to put a strong effort and structure around making sure that we're being able to meet those needs and make sure that we're able to promote effectively and introduce new products.

As you know, we're developing a lot of new products every year, we're entering into new categories, and we continue to see the Internet channel as a good opportunity as they continue to increase their share overall in the consumption side of things.

<Q – Pete Benedict – Robert W. Baird & Co., Inc.>: Okay. Thanks. That's helpful, Scott. Moving over to the gross margin line, again, sticking within HB. You talked about pricing being positive for you guys. Just help us to understand the negotiation process here, you've got input costs coming up, and I'm thinking more on like items. I understand moving to premium can be a pricing net benefit. But on like items, are you able to pass these input costs on right now? Are you passing maybe even a little bit more and being able to expand margin from that standpoint?

I mean, I asked that question because clearly a lot of these major retailers are involved in varying levels of price investment right now across the market. So, just trying to square all that up and see how your negotiations are going and your ability to pass on these input costs are going, at least at this point.

<A – Greg Trepp – Hamilton Beach Brands Holding Co.>: I'll make one quick comment on gross margin, and Scott can talk about the pricing process. But when we look forward and talk about our goal to get $750 million to $1 billion, 9% to 10% op profit, we really model that in a number of ways. But we always try to keep our gross margin in that historical range. You look back overtime, you can see we've really been in a certain range for some time. And we know that there are quarter-by-quarter ups and downs, but we feel pretty good about the fact that we can keep in that range.

So, I think as we go forward, our assumption is it's going to always equalize itself into that. There are some scenarios where the mix wouldn't change enough, but it could go higher than that. But we're assuming that it's going to stay in that historical range. So, as far as the price increase process, Scott, you can talk about that.

<A – Scott Tidey – Hamilton Beach Brands Inc.>: Sure. Looking at the North American market, I think in both these markets we are actively working with our retailers to offset the input costs that we're getting. And so we are working with them, we're picking our spots. It's beneficial to be in 50-plus categories and we've got some depth in those categories.

So, it allows us to change-out products where needed. In some cases, we need to take increases; in some cases, we can change-out products. In other cases, we can also change the way we want to promote our products. So, we can pick things that work better in our margin structure.

But it is fairly collaborative with the retailers. We want to keep them whole and make sure it works for their plans. So, we're working with them to where we can move retails up in the marketplace and then not impact sales.

I would say for the most part, our retailers are seeing these increases from everybody. They also source themselves directly from China. So, they understand that these costs are coming. So, it's just a matter of trying to balance out where is the best place to do it, and how to not impact your revenue.

<Q – Pete Benedict – Robert W. Baird & Co., Inc.>: Okay. That's helpful. Makes sense. Sticking with the cost side, just transportation cost headwind is a hot topic right now in the market. Can you tell us what you guys have been seeing from that? And how that's expected to trend over the balance of the years, as you make your plans?

<A – Jim Taylor – Hamilton Beach Brands Holding Co.>: Yeah, Peter, this is Jim. We're seeing some increases, but not significant and like Scott indicated that goes into the basket of the total input costs and making sure that we cover those in the appropriate way.

<Q – Pete Benedict – Robert W. Baird & Co., Inc.>: Okay that's helpful. And then last, just on the inventory at HB, obviously it was up big this quarter. How does that trend from here? How should we be thinking about a normalized level of inventory growth as we look over the balance of the year?

<A – Greg Trepp – Hamilton Beach Brands Holding Co.>: Yeah. Well, Peter, you just can imagine, the first quarter is always a bit challenging from an inventory planning perspective, due in large part to the supplier shutdowns during Chinese New Year. And some uncertainly as to retailer planning and demand and order flow coming out the holiday season.

So, we did a couple of things to address this. We planned an increase in safety stock levels to ensure we optimized our customer service levels. In addition, our sales forecast for the first half was solid, but the actual demand, while reasonably strong in Q1, came in a bit below the forecast.

And finally, the carrying value of our inventory is higher based on product mix. So, having said all this our inventory levels within a quarter are higher than we would like, but the quality of inventory is good. And I would expect to be in more normalized inventory level as we roll into Q2 and Q3.

<Q – Pete Benedict – Robert W. Baird & Co., Inc.>: Okay. That's great color. My last question is just, you talked about on the revenue obviously you're expecting some deceleration from that, call it, nearly 10% growth rate here in the first quarter. How about from a gross margin standpoint? I mean, it is a very healthy gross margin increase in the first quarter, should we be expecting that to continue or to moderate similarly as we go across the year? And I guess maybe another way of asking is, do you expect your gross margins to be up, I guess, in all quarters across 2018, just maybe not up at the same level you saw in the first quarter? That's my last question.

<A – Greg Trepp – Hamilton Beach Brands Holding Co.>: I think it goes back to one of the earlier comments I made Peter, which is really while we would certainly like them to be higher, it really depends on the mix and how things flow through. Our assumption is they're going to fall back into a historical range.

We don't expect them to go below that range either. But there certainly is a chance that it could be a plus or minus, that historical range. But all signs point to being just us being able to deliver and keep those margins where they've been in the past.

<Q – Pete Benedict – Robert W. Baird & Co., Inc.>: Okay. That's good. All right, guys. Listen, thank you very much. I appreciate the color.

<A – Jim Taylor – Hamilton Beach Brands Holding Co.>: Thank you, Peter.

Operator: Thank you. I would now like to turn the conference back over to Mr. Greg Trepp, CEO.

Gregory H. Trepp, President and Chief Executive Officer, Hamilton Beach Brands Holding Co.

Thank you. As you've heard this morning, we're pleased to get the year off to a good start. We are encouraged by the advances Hamilton Beach made in the first quarter on our strategic revenue growth initiatives, and we expect our progress to continue.

As Kitchen Collection continues to operate in a difficult retail environment, we are working to further right-size the business and better position it to deliver acceptable returns. We're focused on increasing shareholder value over the long-term across both businesses.

But before signing off, I'd like to note that we will be presenting at the RW Baird Consumer Technology & Services Conference in New York on Wednesday, June 6, at 3:45 PM. We hope to see some of you there. That concludes our call today. Thank you for joining us.

Operator: Thank you for participating in today's Hamilton Beach Brands Holding Q1 2018 earnings conference call. This call will be available for replay beginning at 12:30 PM Eastern Time today through 11:59 PM Eastern on May 10, 2018. The conference ID number for the replay is 2184489. The number to dial for the replay is 855-859-2056. This concludes today's conference call. You may now disconnect.

