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MSA - Q1 2018 MSA Safety Inc Earnings Call

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the MSA First Quarter Earnings Call. (Operator Instructions) It is now my pleasure to introduce your host, Elyse Lorenzato, Director of Investor Relations. Please begin, Elyse.

Elyse Lorenzato - *MSA Safety Incorporated - Director of IR*

Thank you, Kelly. Good morning, everyone, and welcome to MSA's first quarter earnings call for 2018. With me here today are Bill Lambert, Chairman and Chief Executive Officer; Ken Krause, Senior Vice President, Chief Financial Officer and Treasurer; and Nish Vartanian, President and Chief Operating Officer.

Our first quarter press release was issued last night and is available on the MSA website at www.MSAsafety.com. Before we begin, I'd like to remind everyone that the matters discussed on this call, excluding historical information, are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements include, but are not limited to, all projections and anticipated levels of future performance.

Forward-looking statements involve risks, uncertainties and other factors that may cause our actual results to differ materially from those discussed here. These risks, uncertainties and other factors are detailed in our filings with the Securities and Exchange Commission, including our most recent Form 10-K filed in February 2018.

MSA undertakes no duty to publicly update any forward-looking statements made on this call, except as required by law. We've included certain non-GAAP financial measures as part of our discussion this morning. Reconciliations to the most directly comparable GAAP measures are available on our Investor Relations website at investors.msasafety.com.

With that, I will turn the call over to our Chairman and CEO, Bill Lambert.

William M. Lambert - *MSA Safety Incorporated - Chairman & CEO*

Thank you very much, Elyse, and good morning, everyone. As always, I want to begin by saying thank you for joining us this morning and for your continued interest in MSA. As you saw in our press release that was issued last night, first quarter revenue increased by 23% on a reported basis or 7% on an organic constant currency basis. We leveraged that revenue growth into $1.01 of adjusted earnings per share, reflecting an increase of more than 70% from a year ago. In fact, EPS on both the GAAP and adjusted basis is a record high for us in the first quarter. So naturally, I'm very pleased with the strong start to 2018.

At our Investor Day in New York City last month, we talked at length about executing what we call our growth and focus initiative throughout 2018. This initiative revolves around 4 key pillars: achieving market leadership positions, driving profitable growth, strategically deploying capital and investing in our talent to support a high-performance culture. From top to bottom across our various regions and functions, our team has embraced that vision and hit the ground running in the first quarter. Today, Nish Vartanian will review our quarterly performance with you, and he'll discuss the key trends we are seeing in our end markets. Then Ken Krause will lead us through our financial review. After that, we'll open up the call for your questions.

Before I hand the call over to Nish, I want to say a few words about our upcoming management transition. As I announced back in December and discussed on our February earnings call and our Investor Day presentation last month, my intention is to step down as CEO of MSA in May and retire as a full-time associate of the company. As we've mentioned on several occasions, the board and I expect to elect Nish Vartanian, our next Chief Executive Officer. Nish and I have been working closely together throughout this succession process to ensure a smooth transition. And the board and I have complete confidence that he is well prepared to lead MSA into the future.

Nish's 32-year history with MSA and within the safety industry, his growth-focused mindset and his well-honed leadership skills will motivate and inspire our associates to continue driving our business forward.

As for my own plans, I will remain a Director and shareholder of MSA. MSA's mission of protecting the health and safety of workers is one I have been very proud to be associated with for nearly 40 years, and I have been honored to lead this organization for the past decade. At the beginning of my tenure as CEO, our revenue was less than $900 million, our operating margin was about 9%, and the trough of The Great Recession was just 9 months ahead of us.

In 2017, our revenue was $1.2 billion, and our operating margin is now trending between 16% and 19%. We have developed world-class technologies, introduced groundbreaking products and acquired assets that have helped us establish market-leading positions in key markets and geographies, like the U.S. fire service, upstream oil and gas and fall protection engineered systems, just to name a few.

We are working more closely with customers than ever before, gathering voice of the customer feedback that enables us to develop and deliver the innovative safety solutions that in turn allow our customers to focus on their core operations and run their businesses more efficiently, while better protecting their workers. We began executing on our core product strategy in 2009. And since that time, we've provided a total shareholder return of more than 300%, far outpacing the major market benchmarks as well as our proxy peer group median. Needless to say, I feel extremely privileged to have had the opportunity to lead this great organization as CEO for the past decade, and as Chairman the past 3 years. But I also feel fortunate to have had a great team right alongside me. And that includes having Nish Vartanian on this great team for the past 32 years. The Board of Directors and I have great confidence MSA will continue to be successful under Nish's guidance and his leadership, and we look forward to seeing his impact.

So with that, I'll turn the call over to Nish Vartanian to discuss our fine performance in the first quarter of 2018. Nish?

Nishan J. Vartanian - *MSA Safety Incorporated - President, COO & Director*

Thanks, Bill, and thank you once again, not only for the confidence that you and the board have placed in me, but also for your input, your guidance and counsel as we continue through this management transition. As Bill noted, 2018 is off to a strong start, and I look forward to continuing to build on the momentum that our entire MSA team has created through the first quarter. Our growth and focus platform, that Bill mentioned earlier, is yielding strong results across our portfolio. And those results are evident in our profitability profile. Overall, the team is doing an excellent job in executing our corporate strategy.

On that note, I'd like to walk you through a few areas of performance for the quarter and highlight some of the trends we're seeing in our key products and markets. Our total sales increased 23% in the first quarter and reflect a record Q1 result for MSA. Excluding an FX tailwind of 5% and the revenue contribution from the acquisition of Globe, constant currency organic revenue increased 7% in the quarter. Not only did we see a strong uptick in revenue this quarter, we also finished with the backlog trending up about 10% from the end of 2017. While backlog can fluctuate due to seasonality, it's encouraging to see the balance trending higher during the quarter where we've achieved significant revenue growth. Similar to Q4, this traction of momentum continues to be broad based among fire service, gas detection, and industrial core PPE products.

Looking more closely at our revenue results, core products led the way with growth of 23% in the quarter. Revenue in firefighter safety increased by 39%, or 4% when you exclude the acquisition of Globe. SCBA revenue was up mid-single digits, and we continue to see strength in the order book in the U.S., and notably also in our international markets in the first quarter.

As you may have seen in our press release issued earlier this month, we secured a $10 million contract to provide G1 SCBA and accessories to the Metropolitan Fire Brigade and Country Fire Authority of Victoria, Australia, 2 of the country's largest fire departments. Not only does this order reflect our largest G1 competitive conversion to date, it reflects our single largest G1 order to date. This is great work by Bob Leenen, Sankalp Navjivan and our Pacific Asia Fire Service sales team. As we noted in the related press release, we expect to ship the majority of that order in the second half of this year.

Looking now at the gas detection area of our core products. In the first quarter, we saw double-digit growth in both portable gas detection and fixed gas and flame detection or FGFD. Portable gas detection revenue increased by 12% on strong base business across the globe. In fact, our incoming orders in portable gas detection approximated the levels we saw throughout 2014. With oil above $65 a barrel and U.S. oil and gas rig count surpassing 1,000 for the first time in 3 years, we see positive momentum for the gas detection part of our business. In FGFD, we saw an increase of 14% in the quarter, also spread relatively evenly between our segments. This performance highlights how our R&D investments are yielding strong returns. More specifically, sales of our next-generation transmitter, the ULTIMA X5000 and S5000 gas monitors contributed meaningfully to the growth in FGFD revenue this quarter. As we discussed at Investors Day, this revolutionary new platform utilizes TruCal sensor technology to provide increased safety and durability, while reducing the overall cost of ownership for our customers. And it's certainly hitting the mark with our customers in the oil and gas market.

With regard to our industrial core product business, we continue to see good demand and realized 11% revenue growth in both industrial head protection and fall protection in the quarter. We've talked before about the industrial head protection business being indicative of the economic strength in growth across industrial applications. And in the first quarter, we saw double digit head protection growth in just about every one of our regions. Similar to portable gas detection, our head protection orders exceeded levels we saw in 2014 at the height of the last commodity cycle. A healthy turnaround cycle is underway in our refinery sector, and the most recent ISN Manufacturing Index of 59 indicates growth in the manufacturing sector. And we're seeing these trends clearly reflected in our order book.

Looking more closely at our fall protection business, sales in this area increased 11% in the quarter, with a 24% increase in the Americas segment, driven largely by the favorable market dynamics I just mentioned, along with good opportunities in construction, power transmission, utilities and the aviation markets. International fall protection posted a 1% decline in the quarter on a difficult large order comp in Australia. However, digging a bit deeper into this story, our European region realized an 11% increase in fall protection revenue, as we drove conversion of engineered systems orders at Latchways. In fact, our European region had overall sales growth of 6%, with good performance across industrial and fire service markets. Certainly, we view this as a nice strong start to the year in the region. We're very much focused on driving improved performance.

I should also note that the 300 basis point operating margin improvement we realized in our International segment this quarter, largely reflects improved profitability in Europe as well as revenue increases in all of our emerging market regions.

In summary, the order pace is very healthy and our backlog is up about 10% from year-end and running significantly higher than this time a year ago. We're seeing healthy conditions in our industrial end markets and realizing some nice wins in the fire services inside and outside of the U.S.

With this significant level of backlog, strong Q1 performance and favorable macro conditions in many of our end markets, we continue to plan for mid-single digit organic revenue growth for the full year of 2018. With that, I'll turn the call over to Ken for his financial review. Ken?

Kenneth D. Krause - *MSA Safety Incorporated - Senior VP, CFO & Treasurer*

Thank you, Nish, and good morning, everyone. Let's start with a few financial highlights. Our organic revenue increase of 7% is on track with the mid-single digit growth expectations that we communicated earlier this year. Incremental operating margin exceeded 35% in the quarter, supporting quarterly adjusted operating margin of 16.8%, a record for the first quarter. The 430 basis point increase in adjusted operating margin was largely driven by leverage on our streamlined cost structure as well as gross profit improvements. GAAP earnings were $32 million and adjusted earnings were $39 million, or $1.01 per diluted share, both measures increasing at more than 3x the 23% increase in GAAP revenue.

Now I'd like to take some time to walk you through our quarterly financial results. Total revenue increased 18% in the quarter in constant currency, or 7% on an organic basis, when we exclude the impact of Globe. Solid performance in every core product line drove 10% core sales organic growth. Gross profit was up 20 basis points in the quarter, expanding on lower indirect manufacturing cost, despite a 140 basis points of dilution from Globe product mix. While Globe was dilutive to gross margin, it was accretive to operating margins by 50 basis points. SG&A expense was $80 million in the quarter, or 24.6% of sales compared to an average first quarter run rate of 29.5% of sales over the past 3 years. In organic constant currency terms, SG&A was flat for the quarter compared to a year ago on the 7% constant currency organic revenue growth. As I mentioned at Investor Day, we continue to focus on controlling discretionary cost and driving productivity and efficiency, while deploying capital for strategic investments that will drive profitable growth, such as the Globe acquisition, which has contributed nearly $0.20 of GAAP earnings over the past 8 months.

GAAP operating income was $44 million and GAAP operating margins were 13.6% in the quarter, up 660 basis points. Excluding foreign exchange, restructuring, strategic transaction costs and product liability expense, adjusted operating margin was 16.8%, improving 430 basis points from a year ago.

As I highlighted on the February earnings call, we adopted the new accounting standard for pension accounting, which indicates that all components of net periodic benefit cost, except for service cost, should be recorded outside of operating income. The result of this change in the first quarter was that we have just over $1 million of pension income, recorded below the operating income line, driving a 40 basis point negative impact on operating margin. Again, this change has no impact on earnings, only a classification change out of operating income or EBIT. Quarterly adjusted EBITDA increased 54% to $64 million or 19.7% of sales compared to 15.7% a year ago. On a trailing 12-month basis, adjusted EBITDA is up 20% to over $250 million or 20% of sales versus 18% of sales a year ago.

Our GAAP effective tax rate was 22.6% for the quarter, which includes just under $1 million of windfall benefit from stock compensation. On an adjusted basis, our ETR was 24.8% compared to 27.8% a year ago, reflecting the benefits of U.S. tax reform. In addition to the lower effective tax rate, tax reform has provided us with flexibility to repatriate foreign cash. In the first quarter, we repatriated $14 million. We are planning to repatriate between $75 million and $100 million for the full year, as I've mentioned in the past. We plan to continue to employ a balanced capital allocation strategy that prioritizes growth investments and also funding our dividend and servicing debt obligations. The repatriation provides us with more flexibility to execute strategic investments that will add value to MSA in coming years.

GAAP net income was $32 million, more than doubling from the quarter a year ago. Adjusted earnings increased 76% to $39 million or $1.01 per share compared to $0.58 per share a year ago. If we look back over the past 3 years, our average adjusted earnings in the first quarter has been about $0.50. We've seen a clear step change in our profitability, and the earnings growth was driven by core product growth, accretive acquisitions, a streamlined cost structure and tax planning and reform-related activities. Free cash flow was $14 million in the quarter compared to $95 million a year ago. And as you may remember, we had about $84 million of net inflows from insurance receivables in the first quarter of 2017, compared to net inflows of $12 million in the first quarter of this year. We used cash for working capital to support the stronger quarterly revenue and order performance. Our debt-to-EBITDA was just over 1.8x compared to 2x at year-end. I'm pleased with the results in the first quarter, and even more importantly, the strength of the order book in both industrial and fire service markets is certainly encouraging. While backlog can fluctuate due to seasonality, it is up to start the second quarter on the improved order pace. We continue to plan for mid-single digit organic revenue growth for the full year of 2018, as we discussed with you on our call back in February. With that, I'll turn the call over to Bill for some concluding commentary. Bill?

William M. Lambert - *MSA Safety Incorporated - Chairman & CEO*

Thanks very much, Ken. As I mentioned earlier, I'm pleased with the strong start to 2018 and the positive trends we are seeing in many of our end markets. As our business and end market stand now, our revenue growth focus is gaining solid traction with earnings seeing the further benefit from good cost control and U.S. tax reform. With that, we're realizing record levels of profitability for the company. To keep this momentum going in 2018, we remain focused on managing discretionary costs, while investing in the areas that will help us capitalize on this current growth cycle. Nish, Ken and the executive leadership team are very focused on executing our growth-focused corporate strategy and driving higher levels of shareholder value in 2018 and beyond. Thank you, again, for your attention this morning. At this time, we will be happy to take any questions you may have. Please remember that MSA does not give guidance, and that precludes most detailed discussions related to our expectations for future sales and earnings. Having said that, we will now open up the call for your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question we have is from Matthew Gall from Barrington Research.

Matthew Ian Gall - *Barrington Research Associates, Inc., Research Division - Senior VP & Senior Investment Analyst*

Couple of things that were positive that I noted, especially in the Europe region which had faced some challenges up in pretty much every product category, at least on a reported basis and even on a constant currency nearly double digit. With fall protection, I know that, that was pointed out by you Nish, but is there anything specifically that you're seeing in terms of longer term trend for that fall protection business? And Latchways can continue its growth where it experienced in Q1?

Nishan J. Vartanian - *MSA Safety Incorporated - President, COO & Director*

Yes. So we had real nice growth in Europe, and that's where we were quite pleased, I mentioned I think of around 11% revenue growth just in our European segment. We really had a very large order last year and the first quarter in Australia that was difficult to overcome for the international region. But overall, the business is in good shape. It's intact. And we expect to see some good performance going forward.

Matthew Ian Gall - *Barrington Research Associates, Inc., Research Division - Senior VP & Senior Investment Analyst*

Good. Good. And then as you mentioned Australia in general, and you have the recent announcement with your largest SCBA order. Is the international fire safety order -- the order size any different than it is in the Americas? Or is that something consistent if it is larger order, in general is it a longer cycle? -- sales cycle, I should say.

Nishan J. Vartanian - *MSA Safety Incorporated - President, COO & Director*

Yes, I'm not sure if I fully understand the question, but the -- it's obviously a very large order, $10 million. It's the largest single G1 order we've received. And that's the nature of the business for Australia. You tend to get very large orders. There are very few fire departments. Where there are thousands of fire departments here in the U.S. market, the Australian market tends to be made up of very large departments and there are fewer purchases. So lots of very big order, and obviously, it's the largest department in Australia. It's not unusual to get those significant orders in Australia because of the size of those departments.

Matthew Ian Gall - *Barrington Research Associates, Inc., Research Division - Senior VP & Senior Investment Analyst*

Got it. Got it. And then within the fixed gas and flame detection, you pointed out that the new product, the ULTIMA and ULTIMA 5000, I believe, transmitter contributed meaningful -- contributed meaningfully in the quarter. Was that ahead of expectations? And is there just a lot more demand with some of the technology that you have there?

Nishan J. Vartanian - *MSA Safety Incorporated - President, COO & Director*

So it's a combination of things. The market's in pretty good shape, as I discussed. So -- and the product showing a little better than anticipated, quite frankly. We're doing a little better on some of the conversions in the marketplace. The customers are really seeing some of the value and some of the features we built into the product. So it's a combination of having some win to our back with the economy in good shape and the budget's in pretty good shape with our customers and their spend. And we hit the market with a product that's really attractive to them. They really like the features of lower maintenance and lower cost of ownership of the product, higher performance. And we've done quite well with that. What we've seen is that the levels of our ULTIMA, the legacy product that we have in place, those sales remain pretty level with what they were a year ago, what we saw with the X and S5000 was really incremental, which was really encouraging for us.

Matthew Ian Gall - *Barrington Research Associates, Inc., Research Division - Senior VP & Senior Investment Analyst*

And then switching over maybe to the cost -- to the expense side. Ken, looking at the SG&A range -- or the SG&A that was reported in the quarter, year-over-year as a percentage of sales, a pretty drastic improvement, and so congratulations there. But I did notice just being up sequentially by $4.5 million to $5 million, just wanted to see if that is something that's indicative more of a range for the year from a dollar perspective? Is there anything in Q1 to point out that might cause that to be higher than where it had been tracking at the latter part of last year?

Kenneth D. Krause - *MSA Safety Incorporated - Senior VP, CFO & Treasurer*

Yes, Matt, thanks for the question. The biggest impact in the first quarter relates to stock compensation, the grants of stock compensation and the vesting provisions around the grant. And so the first quarter, historically, is our heaviest quarter in terms of SG&A expense, and notably related to the stock compensation grants that occur in February of each year, though we've seen a bit of a step, just like we have over the last several years. We continue to look at the cost structure, we continue to manage it. But at the same time, we are investing to realize growth in this market where we're seeing more stronger growth in some of our end markets. So we are starting to see some investments come in, selling investments. So when you look at the quarter, specifically look at the quarter and the SG&A performance in the quarter, it was flat year-over-year on an organic basis. But if you exclude some of the selling investments we've made, some of the commissions on some of the higher FGFD sales, we actually saw about a $2 million reduction in back office and administrative expenses. And so we're continuing to manage the cost structure just like we have over the last several years.

Matthew Ian Gall - *Barrington Research Associates, Inc., Research Division - Senior VP & Senior Investment Analyst*

Bill, best of luck in your future endeavors.

William M. Lambert - *MSA Safety Incorporated - Chairman & CEO*

Thanks very much, Matt.

Operator

And our next question we have is from Stanley Elliott from Stifel Nicolaus.

Stanley Stoker Elliott - *Stifel, Nicolaus & Company, Incorporated, Research Division - VP & Analyst*

A quick question, and I apologize if you had touched on it earlier, I got on a tad late. But can you talk a little bit more about the profitability in the international business up 300 basis points. Is that a function of mix? Or is that really a function of some of the things that you all had talked about at the Analyst Day and trying to improve the profitability there?

William M. Lambert - *MSA Safety Incorporated - Chairman & CEO*

Well, I'll chime in, and Bob is on the call. And Bob if you'd like to add any more color, feel free. At the Investor Day, we laid out 4 focus areas to improve MSA international performance. We talked about leadership changes that were made and being made. We talked also about realigning the commercial organization, the sales and marketing organizations. We talked about channel's optimization effort that we had going on as well as talking about cost-reduction programs. And those cost-reduction programs had a lot to do broadly across international, but also within the European organization. As Nish mentioned, our European growth -- revenue growth was 6% in constant currency terms. So we're really happy to see growth out of the European segment. And we have made and have completed the key leadership changes across the region. We have made the realignment of our sales and marketing organizations to better align them with the end markets that we have. Many of our U.S.-based sales leaders are spending considerable amounts of time in Europe and working through the channel's optimization strategy. As you know, we've had great success here in the Americas with our channel's optimization strategy and we're taking some of that best-in-class type performance and programs and applying that to Europe. And within Europe, we also have the foundation of Europe 2.0, which we completed a few years ago to leverage to further reduce our cost structure and to improve our efficiencies. So we're hitting on all the cylinders, quite frankly, and all the points that we had talked about at the Investor Day a month ago or so. And that Bob has had in place now for the past roughly 9 months. So Bob if there's anything else you'd like to add in that regard? We're seeing good solid performance in each of those areas that you mentioned a month ago.

Bob Willem Leenen - *MSA Safety Incorporated - VP & President of MSA International*

Yes, I think the quarter 1 results are encouraging. As Bill mentioned, the leadership changes and the realigning of the customer-facing organization is largely executed. I think the channels piece is a bit of a -- slightly longer-term play for us, 2 to 3 years because we want to do that very mindfully, capturing both the complexity reduction and the revenue benefits of it. We can see that the channels optimization is working. We're getting traction and expanding relationships with new distributors. We're seeing small end users as part of our customer mix reducing. And frankly speaking, a lot of the revenue growth in Europe in Q1 came from our channel partners. What we also said during the investor conference was that our first priority was getting Europe back to track with revenue growth after 5 quarters of revenue decline, that was the first priority to expand profitability in Europe. I think Q1 results in that respect are encouraging, and then what you'll see is, that management attention will focus a little bit more on mapping out how we're going to have an ongoing path towards optimizing our cost structure in Europe, specifically. I think the Q1 performance for international, that significantly benefited also aside from the revenue growth, significantly benefited from the full year effect of savings we executed last year. And that's why going forward, we'll be digging into that a bit more to make sure we have an ongoing pipeline of improvement in that area.

William M. Lambert - *MSA Safety Incorporated - Chairman & CEO*

Stanley, we gave a lot of guidance at the investor's meeting -- Investor Day meeting. Bob kind of walked through that. And between Bob and Ken, they walked through where the differences are. When you look at our operating margin consolidated, we are roughly 16.9%, just under 17%, as Ken had indicated. For the Americas, where we've had such great success with some of our indirect channel strategies, our cost-reduction programs and efficiency programs, we're running roughly, and I'll talk in whole numbers here, roughly 24% operating margins in the Americas. And International, for the first quarter, is around 11%. So we're now finally into the double digits, but our effort is now to close that gap between international and the Americas, and to further improve consolidated operating margins.

Stanley Stoker Elliott - *Stifel, Nicolaus & Company, Incorporated, Research Division - VP & Analyst*

It certainly was quite impressive. On the input side, are you seeing anything, lots of discussion out there about an inflationary environment, about higher shipping charges, things like that, that you see, either that you had to deal within the quarter or kind on the horizon for you?

Nishan J. Vartanian - *MSA Safety Incorporated - President, COO & Director*

Yes, Stanley, this is Nish. We're seeing some of that. We're seeing some of the shipping expense going up slightly. There's a little bit on our material cost, some increases there, but we're doing a nice job from a pricing standpoint, managing that and we're very mindful of that. So we're watching it very closely. We've got good metrics around it. And we're doing a nice job in managing our way through as evident through our margins. We're doing a really nice job there. And so we'll continue to watch it closely and make adjustments as needed going forward.

Stanley Stoker Elliott - *Stifel, Nicolaus & Company, Incorporated, Research Division - VP & Analyst*

Bill, best of luck to you.

William M. Lambert - *MSA Safety Incorporated - Chairman & CEO*

Thank you, Stan.

Operator

And our next question is from Richard Eastman from Baird.

Richard Charles Eastman - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Nish, could you kind of double back to your comments around Americas, and maybe the SCBA business? You just maybe speak to the backlog there a little bit, if you would. Just -- I'm just kind of looking at the Americas' growth rate in SCBA, and I'm thinking is that seasonality, Is that timing? And maybe just give a little better picture what the backlog looks like going forward?

Nishan J. Vartanian - *MSA Safety Incorporated - President, COO & Director*

Yes. So it's good and strong, Rick. So we -- as we talked about, we had a real strong booking quarter in the fourth quarter, which contributed significantly to the backlog that we have in North American market. We talked about the supply chain, some supply chain issues. So those orders came in late cycle in the fourth quarter. We were caught a little bit off-guard with one of our suppliers not being able to ramp up quickly enough for us to get those out the door. And quite honestly, we did not make a lot of headway with that in the first quarter. As you know, we could have done much better in the first quarter had we worked out the supply chain issues. But our bookings were quite good again in the first quarter. So we really didn't move the needle in making any gains in that backlog. That backlog is still there, and we expect to ship that backlog over the next 2, maybe 3 quarters. We've got to work through the Australian order. We'll have to build some subassemblies here in the second quarter and start to prepare for that, and then make sure we manage that supply chain well. They've ramped up a bit. We're encouraged by what we're seeing with the supply chain in the early part here in the second quarter. But we've got a full good nice sized backlog coming. To put things in perspective, our book-to-bill ratio for SCBA was about 120% in the quarter. So the bookings are still good. And we had an okay first quarter shipping, but it could have been much better had we worked up the supply chain.

Richard Charles Eastman - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Okay. And the book-to-bill you referenced there, that's total, including International and Americas?

Nishan J. Vartanian - *MSA Safety Incorporated - President, COO & Director*

Correct. Right.

Richard Charles Eastman - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Yes. Okay. Okay. And then, just quickly, maybe for Bob. You spoke to this 6% constant currency growth in Europe. And I'm curious if -- I'm not sure how much headway you've made on the distribution side, but is it your sense that the sellout equaled 6%? In other words, the sell-in wasn't a bigger number?

Nishan J. Vartanian - *MSA Safety Incorporated - President, COO & Director*

Rick, why don't -- this is Nish. I'll jump in on that. Yes, so I understand what you're saying. So orders from distribution and sell through for the end user, yes, we're balanced with that. So typically what you see with those industrial distributors, that's pretty balanced. So we're encouraged with what we see and talk about with the European piece. But still a lot of work to do.

Richard Charles Eastman - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Okay. Okay, fair enough. And then just then a quick question on Globe. Again, math serves me -- if the math serves me well, maybe Globe's revenue contribution was about $29 million. I suspect there's no currency in that. I'm curious -- that feels strong to me, is there any seasonality to that number in the first quarter? Or again, is the growth year-over-year, is it double-digit growth at Globe?

Nishan J. Vartanian - *MSA Safety Incorporated - President, COO & Director*

Yes, the business is fairly consistent at Globe, quarter-to-quarter. So that $29 million in your math is pretty good. That $29 million is a good number and it's fairly consistent. It fluctuates a bit due to workdays and some other issues, but that's a relatively good number. And no, I don't believe that's double-digit growth. If we go back to the Globe numbers, it's modest, it's single digit.

Richard Charles Eastman - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Okay. Okay. Fair enough. And any steps there that you could flag to suggest maybe positioning either the product line, the feature set to move that business offshore? Any early steps there, whether it's distribution or just like I said, any product adjustments? Or are we still a year or 2 away from really seeing any international growth for Globe?

Nishan J. Vartanian - *MSA Safety Incorporated - President, COO & Director*

Yes, we continue to look at that. It's -- certainly, we're not going to move any operations offshore for our domestic market. Having that here in the U.S. is important for firefighters and that will stay there. And it's very -- it's very efficient. But we continue to look at those opportunities and we're spending time with fire departments in international and Latin America. In fact, this week at the FDIC, we have some Latin American firefighters coming in and taking a close look at some of the Globe products. And we continue to cultivate those opportunities and look at some other opportunities around the world.

Richard Charles Eastman - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Okay. Okay. And then just last question for Ken. In terms of the cash from operations, again, kind of trying to adjust out the insurance inflow, which is good to see. It sounds like the insurance inflow may be matched in a structured settlement payment in the quarter. But was the timing of the business -- was the timing of the revenue and the shipments in the quarter, did that absorb some of the -- there's some cash and inventory here, there's some cash and receivables, just curious is that a timing issue or receivable...

Kenneth D. Krause - *MSA Safety Incorporated - Senior VP, CFO & Treasurer*

Yes, Rick, it's -- we did have a heavy March, and we saw some good business flow out in March, which hit the receivable number. And then inventory is generally just a build for the backlog that Nish had talked about. So we feel like we're still on track. We're still focused very closely in our working capital management. And so we feel like it'll start to improve here as we go forward. Much of it is also dependent upon just the general -- just the business cycle we're in. And so I've said a number of times, our target is 100% free cash flow conversion of net income. We still are planning for that for this year, but it is dependent upon kind of the growth curve.

Operator

And our next question we have is from Edward Marshall from Sidoti & Company.

Edward James Marshall - *Sidoti & Company, LLC - Research Analyst*

So I wanted to see if there's an update potentially on Globe? I noticed that you (inaudible) $0.20 of GAAP earnings thus far. I want to know if you would like to revise that. I think you're 60% through, which have already hit the high end of (inaudible) business.

Kenneth D. Krause - *MSA Safety Incorporated - Senior VP, CFO & Treasurer*

Yes. It's Ken. It's performing well. I mean, the margins are performing well. We're seeing the synergies come through that business. I think our target of a GAAP basis was $0.15 to $0.20. I mean, I don't see any reason why we won't get to most likely $0.25 for full year on that business. And so we certainly think that's tracking a little bit ahead of the high end of the range.

Edward James Marshall - *Sidoti & Company, LLC - Research Analyst*

Do you think that (inaudible) will carry over the adjusted range as well?

Kenneth D. Krause - *MSA Safety Incorporated - Senior VP, CFO & Treasurer*

Oh, yes, certainly, it will. It certainly will carry through on the adjusted range.

Edward James Marshall - *Sidoti & Company, LLC - Research Analyst*

Okay. And Stanley had talked about the international business earlier. And I just wanted to ask one more question on that. If we could talk about maybe the structure of the international business as it relates to maybe the Americas. Obviously, I don't think it has the structure to be -- given the geographic kind of mix and the regional mix there, probably can't reach the Americas. But is it 70% of the Americas as far as the margins once you're kind of through this? I mean, what are you guys targeting for the international business from a margin perspective?

Kenneth D. Krause - *MSA Safety Incorporated - Senior VP, CFO & Treasurer*

Ed, we had talked at the Investor Day that there is opportunities on the gross margin, there's also opportunities on the SG&A side. And in the quarter, we essentially executed on both initiatives. That 300-or-so basis points, 2/3 of that's SG&A and 1/3 of that is gross profit. So we -- right now, it's -- we're very early on and we've made significant changes over the last 9 months. We're very early on, but we're tracking very nicely. I mean, we don't think it will ever get -- or in the foreseeable future, it get to a point that the Americas is. But we certainly see opportunities to continue to go higher from this low-double digit range over the next several years.

Edward James Marshall - *Sidoti & Company, LLC - Research Analyst*

More like mid-double digit or mid-teens rather or...

Kenneth D. Krause - *MSA Safety Incorporated - Senior VP, CFO & Treasurer*

Yes, good try. I mean, we're very early on, Ed. It's 1 quarter end. I mean, it's the first quarter, as Bob had said, and a numbers of quarters where we've seen growth come through in the European business. So let us get another quarter or 2 kind of under our belt and continue to reassess the execution that we're seeing in that business and some of the expanded relationships on the industrial side, and we'll be more forthcoming. But I think right now we're just making -- we're making good progress. We're tracking well versus some of our initial expectations.

Edward James Marshall - *Sidoti & Company, LLC - Research Analyst*

I agree. I agree. So competitive conversions in the U.S., are you still seeing -- I know you mentioned the Australian order or the international order, but are you still seeing the competitive conversions in the U.S.?

William M. Lambert - *MSA Safety Incorporated - Chairman & CEO*

Yes, Steve?

Steven C. Blanco - *MSA Safety Incorporated - VP & President of Americas*

Yes, this is Steve Blanco. And I would say, yes, we still continue to be the market share leader. In SCBA, the first quarter, as Nish mentioned, reinforced that. We had a nice quarter on incoming, and we just need to continue to work to convert and ship that backlog. So yes, it's been solid, and we haven't seen any change in that.

Edward James Marshall - *Sidoti & Company, LLC - Research Analyst*

Are you still seeing kind of orders with the add-on devices that go along with it? Or are you seeing that shift now to more on the Globe product line than you are on the SCBA product line?

Steven C. Blanco - *MSA Safety Incorporated - VP & President of Americas*

Well, they are different. So -- I mean, they go if it's a Globe product, the -- what the Globe product does is separate of the SCBA. But we certainly continue to see strong success with accessories and the integrated thermal imaging camera, which we talked about at the Investor Day, has been very, very successful. So yes, that's continued to gain traction. We expect that's going to be a market-leading position for us throughout the year. So it's been really good.

William M. Lambert - *MSA Safety Incorporated - Chairman & CEO*

It's encouraging for us...

Nishan J. Vartanian - *MSA Safety Incorporated - President, COO & Director*

Yes, and what's encouraging for us -- and one of the things we didn't build into Globe was much synergy revenue with the Globe acquisition, and we're beginning to see some of that. So we're seeing some of that, that's not really counted in those Globe numbers that comes in on the MSA side of the business, so to speak. So you don't see that in the Globe P&L. We're seeing that with the few SCBA wins and some additional fire helmet wins. So that's encouraging for us. And that wasn't built in as part of our model so to speak when we made that acquisition. Ken keeps us pretty disciplined there.

Edward James Marshall - *Sidoti & Company, LLC - Research Analyst*

Bill, I wanted to echo the best wishes stated by my peers. I think you've been instrumental to the positive changes in the MSA. And you've built a great team, so you know they are in good -- the company is in good hands, but I've known you for 11 years now, so I'm going to miss working with you. Good luck...

William M. Lambert - *MSA Safety Incorporated - Chairman & CEO*

Thanks very much, Ed. I very much appreciate those comments.

Operator

And our final question of the day is from Brian Rafn from Morgan Dempsey.

Brian Gary Rafn - *Morgan Dempsey Capital Management, LLC - Principal, Director of Research, and Lead Portfolio Manager*

Give me a sense, when you guys look at your SCBA, now that you've gotten out of that [area] of kind of pent-up demand. Are the opportunities in sales for the G1 more international than domestic? Or is it a balance? Or is it difficult to forecast?

Nishan J. Vartanian - *MSA Safety Incorporated - President, COO & Director*

No, no, the pipeline remains quite good in the U.S. So we do a careful analysis of our pipeline, our business and the U.S. business remains -- looks to be pretty good. Our pipeline, it goes out about 18 months where we have pretty good view. Timing is sometimes an issue, where the business gets a little clumpy on the cycle of budgets. But the U.S. business remains good, and we've got a heavy emphasis and focus on the international business. Obviously, as you saw with Australia and there are some other midsized wins, Europe had a good quarter on SCBA. So when we're launching the M1 breathing apparatus later this year, which is focused on the international market. So there's opportunities around the globe. When you think of the Australian order and you think of fire service around the globe, and you think of your major cities throughout the world, MSA has very good representation, a strong brand and there is opportunities for breathing apparatus around the world for us. So we think the pipeline in the future is going to be quite good.

Brian Gary Rafn - *Morgan Dempsey Capital Management, LLC - Principal, Director of Research, and Lead Portfolio Manager*

Nish, is there a different sales cycle between international and domestic? [Give] your sense on what -- how is that sales cycle?

Nishan J. Vartanian - *MSA Safety Incorporated - President, COO & Director*

Not necessarily. So just this week, we had some visitors in from Europe who were looking at making a purchase in 2020, 2021 possibly. So we're beginning to visit manufacturers, and we'll start their process. And that's not unusual for major departments here in North America. It's a long-term commitment that fire departments are making. They take their time, they do thorough evaluations, build relations, obviously, with manufacturers, so they've a level of comfort and support for post-sale support on the product. So the buying cycle is fairly similar here in North America as it is around the world.

Brian Gary Rafn - *Morgan Dempsey Capital Management, LLC - Principal, Director of Research, and Lead Portfolio Manager*

When you look at some of the niche in the fire service, I would say, like, military, U.S. Navy and the carriers, maybe airport fire service, are those viable niches? Or is it primarily just a municipal (inaudible) volunteer fire department?

Nishan J. Vartanian - *MSA Safety Incorporated - President, COO & Director*

No. Well, so the military business is fairly significant. As you pointed out -- as you would imagine with the Air Force, the Army, the Canadian Department of Defense is a major customer of ours. The U.S. Air Force is a major customer of ours. So those are all opportunities. And we do work with different militaries throughout the world for firefighting and fire protection. So that's not only opportunities with the SCBA, but also fire helmets and turnout gear.

Brian Gary Rafn - *Morgan Dempsey Capital Management, LLC - Principal, Director of Research, and Lead Portfolio Manager*

Got you. Can you talk a little bit about the thermal imaging camera on the G1? Is there an ability to add single accessories to G1s that are already out in the field? Or is that primarily a new product sale?

Steven C. Blanco - *MSA Safety Incorporated - VP & President of Americas*

Yes, Brian, this is Steve Blanco. We actually do that. It's a good question. We have a number of iTICs, or the integrated thermal imaging camera that we actually sell to existing G1 customers. So there are roughly 80,000 units we have in the field. A number of those were sold before we actually launched that product. And we continue to see a pretty good take rate from customers. We had a really nice take rate the first year out of the gate. Not quite as high this year, it's now more leaning towards new units, but we still have a number of customers that have a product in the field that are taking the iTIC.

Brian Gary Rafn - *Morgan Dempsey Capital Management, LLC - Principal, Director of Research, and Lead Portfolio Manager*

Got you. You made a comment about market share. Can you put any numbers on that on the SCBA side as we stand here currently?

Steven C. Blanco - *MSA Safety Incorporated - VP & President of Americas*

Yes, we haven't gotten to one, but we've maintained in the mid-40s range that we had. So we've been in really good shape. And we see ourselves right now as the market share leader for North America, Brian.

Brian Gary Rafn - *Morgan Dempsey Capital Management, LLC - Principal, Director of Research, and Lead Portfolio Manager*

Got you. Got you. Nish, can you talk a little bit -- I'm wondering have you seen any cost inflation on the raw materials feedstock side? And then maybe Ken, anything payroll inflation, health care inflation beyond what you'd see normal?

Nishan J. Vartanian - *MSA Safety Incorporated - President, COO & Director*

Yes. So on the material cost, we've seen a little bit. We've seen some, nothing significant, nothing that's not manageable. But -- and we're watching our pricing very carefully. So we have rational competitors in the marketplace. And we believe that as we see some increases, we'll pass some of those along and maintain our margin profile as we go forward. So we're pretty disciplined in that area and watching that very closely.

Kenneth D. Krause - *MSA Safety Incorporated - Senior VP, CFO & Treasurer*

And on the wage inflation, just echoing Nish's comments. We're starting to see a bit of wage inflation, and so we're taking a very close look at price increases and ways that we can mitigate and offset that inflation in our business.

Brian Gary Rafn - *Morgan Dempsey Capital Management, LLC - Principal, Director of Research, and Lead Portfolio Manager*

Got you. Got a question for Bill on the way out here. The whole talk about Trump and tariffs, NAFTA redrafting, exclusion from the TPP. Do any of these structural government trade policy, do they provide any headwinds or strategic challenges for you guys?

William M. Lambert - *MSA Safety Incorporated - Chairman & CEO*

Well, I think that we're seeing really minimal impact from the steel and aluminum tariffs so far. We don't expect to see any meaningful impact to costs in 2018 on that front. At least that's our expectation at this point in time. I think the bigger trend to watch is inflation, which Nish has talked about and you asked questions on. Inflation, and what we're seeing with the cost increases in certain areas of our supply chain and raw materials, electronic components, high-density polyethylene, those are the areas that I think causes greater concern than what we see with regard to the steel and aluminum tariffs so far. The cylinders that we utilize in our SCBA are domestically produced, whether those be steel cylinders or composite cylinders. So it's not really a big impact.

Brian Gary Rafn - *Morgan Dempsey Capital Management, LLC - Principal, Director of Research, and Lead Portfolio Manager*

And then Bill, you mentioned a little bit, talking about the base Europe 2.0, obviously between 11 and 24, that's a pretty big gap. Are there any structural impediments between international and domestic, be it geography, culture or politics, where obviously getting the parity between international and domestic is not going to happen? And how are those challenges to close that gap for you guys from a structural standpoint?

William M. Lambert - *MSA Safety Incorporated - Chairman & CEO*

Well, I think, Ken hit on that quite a bit, quite frankly, Brian. I think that there are structural differences between what we were able to do in the Americas, the U.S. and Canada, in particular, and that broad rest of the world, Europe, Middle East, Africa, Australia, China. There are structural differences in the sense that we can't be quite as efficient as we can be serving the U.S. market or the Canadian market. And so our goal is to close that gap. I think it will be very difficult, at least for me to see at this point in time, that we would ever reach parity between our International segment operating markets and our Americas operating margins. There's just -- it's just too difficult, too different for all the reasons that you mentioned. Whether it be geographic reach, the distances between our plants and our customers, government regulations, statutory requirements in these areas, there's a whole host of reasons. That's not to say though that we don't still see opportunities as Ken mentioned and we talked at length about at the investor meeting -- Investor Day meeting last month. There is opportunity for further improvement there. And we're pleased by the first quarter performance of roughly 11% operating margins, and we expect to see that continue to increase.

Brian Gary Rafn - *Morgan Dempsey Capital Management, LLC - Principal, Director of Research, and Lead Portfolio Manager*

Bill, it's been a real pleasure. Best of luck to you.

William M. Lambert - *MSA Safety Incorporated - Chairman & CEO*

Thank you, Brian. Appreciate that.

Operator

And we have no further questions. So I will turn the program back over to you, Elyse, for final comments.

Elyse Lorenzato - *MSA Safety Incorporated - Director of IR*

Thank you. Seeing that we have no more questions, that will conclude today's call. If you missed a portion of the conference call, an audio replay and transcript will be available on our Investor Relations website for the next 90 days. On behalf of our entire team here, I want to thank you for joining us this morning, and we look forward to talking with you again soon.
