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MSA - Q1 2017 MSA Safety Inc Earnings Call

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CORPORATE PARTICIPANTS

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

Mark Deasy *MSA Safety Incorporated - Director of Corporate Communications*

William M. Lambert *MSA Safety Incorporated - Chairman, CEO and President*

CONFERENCE CALL PARTICIPANTS

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

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

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

Stanley S. Elliott *Stifel, Nicolaus & Company, Incorporated, Research Division - VP and Analyst*

PRESENTATION

Operator

Good day, and welcome to the MSA First Quarter Earnings Call. (Operator Instructions)

It is now my pleasure to introduce your host, Mark Deasy, Director of Corporate Communications. Mark, please begin.

Mark Deasy - *MSA Safety Incorporated - Director of Corporate Communications*

Thank you, Jamie, and good morning, everybody. I too would like to welcome you to our first quarter earnings conference call for 2017.

Leading our call today are Bill Lambert, Chairman, President and Chief Executive Officer; and Ken Krause, Vice President, Chief Financial Officer and Treasurer. Our first quarter press release was issued last night, and it is available on the MSA website at www.msasafety.com.

Before we begin, I need to remind everybody 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 SEC, including our most recent Form 10-K which was filed on February 28 of this year. You are strongly urged to review all such filings for a more detailed discussion of such risks. Our SEC filings can be obtained at no charge at www.sec.gov and on our own website in the Investor Relations section. MSA undertakes no duty to publicly update any forward-looking statements made on this call except as required by law.

In addition, I need to note that as part of our discussion this morning, we have included certain non-GAAP financial measures. These measures should not be considered replacements for GAAP results. Reconciliations to the most directly comparable GAAP measures are likewise available in the Investor Relations section of the MSA website. You can find this information in the quarterly results section which is located under the Financial Information header. That concludes our forward-looking statements.

So with that, it's my pleasure to turn the call over to our Chairman, President and CEO, Bill Lambert. Bill?

William M. Lambert - *MSA Safety Incorporated - Chairman, CEO and President*

Thank you, Mark, 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, in the first quarter, we were able to drive 24% growth in adjusted earnings despite a 5% decline in reported revenue. It's certainly worth noting there were a number of difficult comparisons across several of our product groups, most notably SCBA. And I'll provide more insight into the drivers of our revenue performance in just a moment.

While the top line comparison was challenging overall in the quarter, there were several bright spots that reflect continued strong execution by our team. For instance, we continue to see good order flow in the industrial areas of our business with portable gas detection and industrial head protection posting double-digit revenue increases in the first quarter.

Gross margins showed meaningful improvements as well, as we saw strengthening in substantially all of our product categories. Operating margins continued to show good improvements as we continued our focus on improving the efficiency in our business and realigning our cost structure. And we continue to make good progress in improving free cash flow while driving improvements in working capital and making good strides in collecting our insurance receivable balance. Ken Krause will cover these areas in more detail in his commentary.

Today, I'll discuss the trends we are seeing across our core product business and give you some more insight into one of our recent product launches in the fire service market, the G1 Integrated Thermal Imaging Camera, or what we more commonly call the MSA iTIC. It's expected to be the star of the show at this year's Fire Department Instructors Conference in Indianapolis, or FDIC, which begins tomorrow.

I will talk more about our FDIC plans in just a moment. But before I do, I'd like to take a broader look at MSA's revenue performance in the quarter. Looking closer at our first quarter results in core products, we saw a 3% decline in constant currency compared to a year ago. As I mentioned, it's important to take into consideration various product trends we saw in our key end markets when looking at the total revenue line.

Starting with industrial products. We continued to gain momentum in portable gas detection and industrial head protection this quarter. As we indicated on the February earnings call, we saw strong order trends in the first several weeks of the year, which provided us with a sense of confidence around our low-to-mid single digit organic constant currency revenue growth target that we discussed with you on that call.

I'm pleased to say that the robust order pace has continued, and as a result, we were able to recognize a 13% increase in portable gas detection revenue and a 16% increase in industrial head protection revenue in this first quarter. The strengthening industrial landscape is supporting the higher level of base business in these areas and this is providing a nice mix tailwind to our product margins.

Fall protection revenue was down 7% in the quarter, impacted largely by the timing of large shipments in the first quarter of 2016. However, we saw a strong order pace in the quarter, up 10% versus the same quarter a year ago. In fact, our overall fall protection backlog was about 40% higher at the end of the first quarter compared to year-end. And we have the pipeline to continue growing this business.

As we've mentioned in the past, our integration plan for Latchways includes continued expansion of their base business. Building on our success from 2016, we are seeing some nice wins across attractive industries like aerospace, utilities and renewable energy.

In addition to the pickup we are seeing across industrial markets, solid demand from the fire service is also benefiting our order book with our backlog for self-contained breathing apparatus increasing from year-end. I'm pleased to note that this quarter, we achieved our second-highest SCBA incoming order total since we began taking orders for the G1 SCBA. However, that trend is difficult to see in the revenue line due to the tough SCBA comparisons against prior year.

If you remember, we mentioned on the February earnings call that we expected to see difficult comparisons in the first quarter as a result of large orders that we shipped in the first quarter of 2016. While I'm a little disappointed to see the revenue decline this quarter, there are a number of large G1 orders in the backlog for cities like Chicago, San Bernardino and Des Moines, Iowa. Our competitive conversion rate for the G1 continues to trend at just over 50% this year, continuing the trend that we saw throughout 2016. And I'm pleased to say we are not sacrificing profitability for market share gains. Gross margin on SCBA in the Americas segment increased 560 basis points in the quarter.

In addition to realizing benefits from ongoing value-engineering activities and strategic sourcing, we began invoicing for the integrated thermal imaging camera during the quarter, which is accretive to the G1's gross margin and MSA's overall gross margin.

For those of you on the call who may not have heard us talk about this new technology, the MSA Integrated Thermal Imaging Camera for our G1 SCBA platform makes the concept of personal thermal imaging a reality. First and foremost, it is the only unit on the market that is built directly into a firefighter's SCBA. This design provides multiple advantages for the firefighter, such as an auto-on feature that activates the camera once the SCBA is pressurized. Second, the iTIC is driven by G1 SCBA single integrated power source, which eliminates the need for additional batteries, which further reduces a fire department's total cost of ownership over the life of the SCBA, which is obviously a key value proposition for us.

But perhaps most importantly, this revolutionary product gives fire departments the opportunity to cost effectively equip every firefighter with thermal imaging technology. As I've mentioned in the past, we do not view the G1 SCBA as just a product. Our strategy in this area is all about leveraging the versatile and adaptable G1 platform in ways that allow us to bring new technologies to the market faster while expanding our market share.

At the FDIC show this week, this new iTIC offering will be the major focal point of the MSA exhibit. With over 30,000 firefighters expected to attend the show, the FDIC conference provides the ultimate stage for demonstrating how MSA's iTIC can save lives while changing the way fires are fought.

In fact, to help our customers appreciate and see the potential of this new technology, we will be providing show attendees with a fully immersive virtual reality experience featuring the G1 iTIC in a number of firefighting scenarios. As our marketing theme for the FDIC conveys, our goal is to provide vision and safety for all with this new innovation. And we're proud to be at the forefront of the revolutionary technology.

So whether we are bringing advanced technologies to the fire service market or developing new state-of-the-art FGFD platforms, like our Ultima X5000 and S5000 gas monitors for the energy and industrial sectors, which just launched this week, our associates around the world live by MSA's core values every day. And at the center of this culture is our foundational core value of integrity.

Because of our associates' commitment to our values, we were once again recognized by the Ethisphere Institute as a World's Most Ethical Company for 2017, marking the third consecutive year MSA has earned this distinction. And of the 124 companies recognized this year, MSA is 1 of only 4 U.S. industrial manufacturing companies to be honored. And we were the only company recognized in the security and protective services category. This award truly belongs to our 4,300 associates around the world who personify MSA's values each and every day. And to them, I say thank you.

With that, I'd like to turn the call over to Ken for his financial review. Ken?

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

Thanks, Bill, and good morning, everyone. I'd like to take some time and to walk you through our financial results and to provide more insight into the drivers of performance. Additional information will be available when we file our Form 10-Q with the Securities and Exchange Commission.

Let's start with a few highlights, and then we'll take a closer look at the quarterly performance drivers. Despite the challenging comparison in revenue in the first quarter resulting from large SCBA and ballistic helmet orders a year ago, we saw strong improvements in some of the most profitable areas of our business in the quarter.

Revenue from portable gas detection and industrial head protection were up 13% and 16%, respectively, in the quarter on strengthening conditions across the industrial sector. Gross profit of 45% increased 180 basis points from a year ago. As Bill indicated, we saw improvements across substantially all of our core product areas.

As we've talked about on prior calls, we made great progress in streamlining the organization in 2016 with a sharp focus on productivity and efficiency, and we continued to build on that strong foundation in the first quarter. SG&A expense continued to reflect that focus, decreasing by $3 million or 4% from a year ago despite higher spending of about $3 million associated with strategic projects, stock compensation and legal expense related to the insurance recovery program.

The focus on value creation across our business drove an improvement of 110 basis points in operating margins from a year ago and an improvement of 14% in net income and a 24% increase in adjusted earnings. Quarterly free cash flow was $95 million compared to a use of cash of $17 million a year ago. While collections on our insurance-related receivables drove a portion of this, we continued to see good progress on the working capital front.

Looking closer at the insurance-related receivables, we continued to make great strides in collecting these in the quarter. To give you a better sense as to our progress, let's walk through the receivable balance over the past several quarters. If you remember, at the end of the third quarter of last year, we had $155 million in insurance receivables and $104 million in notes, equating to total receivables related to this matter of just under $260 million. Since then, we have made solid progress and have insurance receivables of just under $60 million and notes of just over $80 million at the end of the first quarter or approximately $140 million in total receivables related to this issue.

From a cash standpoint, we have collected $125 million from insurance recoveries since the third quarter of 2016. Additionally, earlier this month, we resolved, through negotiated settlements, certain coverage litigation with multiple carriers and will receive cash payments of $14 million in the first quarter of 2018. Those amounts will be reported as reductions from the insurance receivable in the second quarter of 2017.

These recent settlements, combined with past settlements, should provide cash flow of $20 million to $25 million for the remainder of 2017 and another $20 million to $25 million in 2018.

Now let me walk you through the quarterly financial results. Constant currency sales were down 4% in the first quarter. We expected a difficult comparison in SCBA and ballistic helmets on large orders shipped in the prior year, and that is exactly what we saw. Offsetting the declines in SCBA and ballistic helmets were strong improvements in the industrial sector, notably within head protection and portable gas detection. We saw double-digit increases in revenue in these areas in the quarter and order pace has remained strong through April.

As we've mentioned in the past, these products have shorter lead times and have historically been a solid indicator of trends to come in the industrial sector. First quarter orders in short-cycle industrial products, like head protection and portable gas detection, reached their highest point since the first quarter of 2014. If you recall, oil was close to a $100 a barrel at that time. Certainly good to see orders in these areas coming in and starting to show sustainable signs of recovery.

And while these products are leading indicators, FGFD can be thought of as a lagging indicator. Demand in the Americas segment remained soft in this area on sluggish project spending, but we continue to see strong trends in parts of the world where the cost of oil extraction is lower, like the Middle East. In fact, while revenue in this area was down in the quarter, our backlog is healthy with quarterly FGFD orders in the Middle East increasing 30%.

Gross profit continues to be a bright spot in our results, finishing 180 basis points higher than a year ago.

We saw a nice tailwind from mix on the uptick in industrial-related products, but we also saw margin improvements across nearly all of our core products in the quarter. As Bill mentioned, one of the more notable increases was in the Americas segment SCBA margins, and that builds on the strong progress we made in 2016 in this area.

We continue to take cost out of our products and find new ways to add value through technology, with the integrated TIC being a prime example. Despite spending $3 million more on legal expense, stock compensation and diligence-related cost, SG&A expense was down 4% or $3 million from a year ago. We continue to plan for $10 million of cost savings in 2017 as a result of the steps we took in 2016 to reduce our cost structure.

In connection with those activities, you may have noticed restructuring spend of $13 million in our income statement for the quarter, primarily related to the voluntary retirement program we offered to employees late last year and completed in February. Nearly all of this program was funded through our overfunded North American pension plan, making it a non-cash charge.

While we continue to evaluate additional streamlining opportunities moving forward, we remain highly committed to making investments that drive leadership positions in our core areas, like R&D. We continued to fund those activities at 4.1% of sales in the quarter, right in the target range of 4% to 4.5% of sales that we've communicated to you in the past.

GAAP operating income was 7.3% of sales in the quarter, which includes the restructuring charges I mentioned a moment ago. Adjusted operating margin excluding restructuring and currency exchange net losses in the first quarter was 12.3% of sales, improving 110 basis points from a year ago.

Our effective tax rate this quarter was 10.9% on a reported basis, which includes a $3 million tax benefit associated with changes in accounting standards for share-based compensation. Excluding this windfall tax from the current year and exit taxes associated with our European reorganization from the prior year, our adjusted tax rate was approximately 28% in the quarter compared to 34.7% a year ago, improving on a more favorable projected profitability profile and nonrecurring tax expense associated with asset sales in the prior year. We expect the ETR to approximate 32% to 33% for the year, down about 100 to 200 basis points from a year ago as we see improvements in the geographic profile of profitability.

Net income from continuing operations was $14 million in the quarter on a GAAP basis compared to $13 million in the same period a year ago, up 14%. Adjusted net income was $22 million, increasing 24% from a year ago on the higher gross profit, the lower cost structure and a more favorable underlying tax rate. This equates to adjusted diluted EPS of $0.58 in the quarter.

Free cash flow performance continues to reflect our ongoing focus on collecting our insurance receivable and improving working capital. Our current year free cash flow includes $85 million of net inflows from insurance collections, while the prior year includes the use of cash of $20 million in this area.

While insurance receipts were a significant driver of the quarterly performance, we also continued to see solid working capital management contributing to higher levels of cash flow. Working capital was 23% of sales at the end of the quarter, improving 300 basis points from this time a year ago.

Our debt balance was $295 million, which is down $95 million from year-end 2016 and down over $180 million from the same quarter a year ago. As we indicated in our recent 8-K filing, we used the $81 million insurance payment we received in the quarter to service outstanding debt on our revolver, lowering debt-to-EBITDA to 1.3x at the end of the quarter compared to 1.8x at year end.

Our capital allocation priorities remain consistent moving forward. We will use cash first and foremost to grow our business while continuing to fund an increasing dividend and servicing debt obligations. We're evaluating a number of growth strategies and look forward to using our additional capacity to make investments that help capture market share and drive value.

Before I turn back over to Bill, I wanted to make a few concluding comments. While there were challenges in the quarterly revenue comparison as expected and communicated to you in February, we saw very positive trends in order activity and in industrial-related markets. Our backlog is healthy to start the second quarter, and order activity in industrial products continues to provide a sense of optimism.

Also, we continued to make good progress improving productivity. The continued gross margin expansion and ongoing SG&A reduction drove growth of 24% in adjusted earnings in the quarter and provides opportunities for further profitability improvements.

Driving free cash flow remains a top priority in 2017, and we are off to a great start. We've made good strides in securing and receiving payment on our insurance-related receivables and continue to build momentum in improving the management of working capital.

I will now turn the call back over to Bill for some concluding commentary. Bill?

William M. Lambert - *MSA Safety Incorporated - Chairman, CEO and President*

Thank you, Ken. Despite some of the challenges we faced in the quarter on the top line, as Ken indicated, we were able to grow adjusted earnings by 24% and drive higher levels of free cash flow. I was really pleased by this.

Looking forward, we are seeing encouraging signs across our industrial markets, and our order book mirrors the positive macro trends we are tracking with our channel partners. Energy markets appear to have stabilized and rig count continues to increase, downstream refiners are projecting higher levels of turnaround investment for 2017 and utilities are expected to continue investing in grid modernization and infrastructure upgrade projects. Overall, the fundamentals and key drivers of MSA's business are starting to point in the right direction.

That said, we operate across a number of end markets and geographies that remain uneven and a bit volatile. And with this perspective in mind, we continue to feel that low to mid single digit revenue growth for 2017 is a reasonable target in this environment, and we will be working diligently toward that goal throughout the year.

As I noted in my letter to shareholders in our recently released annual report, we make great strides in 2016 in increasing shareholder value and generating top-quartile shareholder returns compared to our benchmark group. We're certainly proud of that performance, but there is more work ahead and we're not taking our foot off the accelerator. We have a sharp focus on driving profitable growth while continuing to increase value for all of our stakeholders in 2017.

With those comments, thank you for your attention this morning. And at this time, Ken and I will be happy to take any questions that you might have.

Please member that MSA does not give guidance, and that precludes most discussion 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 call is coming from Rick Eastman from Robert W. Baird.

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

Very quickly, could you just kind of speak to the fixed gas and flame business a little bit here? Could you just maybe parse out how the equipment side of that did versus the MRO side? And then also, you did allude to the backlog being -- or order flow being stronger in the quarter. Could you just give us a sense of -- is the backlog at the end of the first quarter, is it up? Down? And maybe just give us a sense of where that business -- or what that business looks like right now.

William M. Lambert - *MSA Safety Incorporated - Chairman, CEO and President*

Yes, Rick, let me give you a little bit of texture, and then Ken can give you the actual numbers here. I think, as Ken indicated, we were seeing some nice, strong growth in international for FGFD, particularly in the Middle East, where, as I think Ken indicated, the cost of oil extraction seems to be lower. And while there are fewer projects than in previous years, there are still projects that are being bid and that we are winning on -- winning in. Our incoming order book for the Middle East, Africa, India region for FGFD was up 28% versus a year ago. So we're seeing some really strong activity, I think, internationally for FGFD. Ken, maybe you have the actual numbers on backlog and what we've seen in the way of backlog in FGFD.

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

Yes, sure. Rick, what we historically see on the backlog side of the business is the fourth quarter certainly comes down considerably as we ship on projects. And then in the first quarter, we see it come back. And so what -- we saw that exact same pattern this year. The first quarter is back at levels that we've seen historically. So the business is -- I would say, is very much still intact with kind of what we've seen over the recent term in terms of performance.

William M. Lambert - *MSA Safety Incorporated - Chairman, CEO and President*

I think the -- to answer your question on the split between MRO and actual new projects, I don't have that level of detail here, but perhaps in a follow-up conversation with Ken, you can take a look at that.

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

Sure. Okay. And then just a question around the international revenue, I think the core organic revenue is down like 9%, high single digits. Can you just give us a perspective on where the tough comps, I believe that was China SCBA comp that was tough, but how does the underlying tone of business there? Is it better than the 9% core decline year-over-year looks?

William M. Lambert - *MSA Safety Incorporated - Chairman, CEO and President*

Yes, I think it is. International was driven primarily by softness that we saw in Europe, quite frankly. And Europe is off to a slower start than what we had expected and the year-over-year comparison in the first quarter is disappointing. We are seeing some lift in the industrial products, like gas detection and head protection over there, where our orders were up 11% in Europe for head protection, up -- excuse me, in gas detection, and up 40% in industrial head protection. But the government funding cycle in Europe has been really challenging, and it's creating a whole lot of uncertainty in the fire service market, particularly in Germany, and then in the military business that we have over in Europe. So that's a little bit behind plan and we're a little bit disappointed with what we've seen there, Rick. But when I look more broadly at international, I don't think I have that same level of concern. Our order book in China, it was up 18% versus a year ago, which was great to see. I indicated already Middle East, Africa region is growing nicely and we're seeing a nice backlog of business start there. So I think, and at least -- Ron is unable to be here today, Ron is traveling, to provide more commentary on international. But I think this was kind of a slow out of the gates for Europe in the first quarter. But we don't expect to see that continue for the balance of the year. Ken anything else you want to add?

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

The only thing also I would add is we've talked about Europe on a number of occasions with respect to the ballistic business. And that's certainly -- as you see the non-core number coming in weaker, that's certainly what we felt in the first quarter in of '17, was just a weaker environment on the ballistic helmet business. And so that's what drove the significant decline in that side.

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

I understand. And then just go -- and then in China sales again, did the -- were China sales in the quarter -- I understand your comment about orders, Bill, but were China sales are also lower given the SCBA comps? Is that part of what we're seeing?

William M. Lambert - *MSA Safety Incorporated - Chairman, CEO and President*

They were lower. They were lower, and it was driven by breathing apparatus sales. You're exactly right.

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

That's exactly right. I mean, the business in China was down predominantly because of breathing apparatus. When we look at the other core products, especially head protection and fire helmets, portable gas, we saw good growth in those businesses in China in the quarter. Double digit lift, yes.

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

Double digit, okay. And then just last question from me, I apologize. The SG&A line, Ken, how does that look for the balance of the year? Do we kind of -- do we essentially work higher off the, you call it, $75 million of SG&A number? And how do we think about that number? Because the biggest piece here was the early retirement program that steps down in total. So do we work higher off the quarters from the $75 million level?

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

Well, we have taken solid steps in the SG&A front. And if we go back to what we've provided in terms of guidance around our cost reduction program, we had talked about our reduction -- our program that was targeted at taking out $10 million of cost out of our cost structure in 2017, again. And so majority of that $10 million is expected to come out of the SG&A line of the P&L, Rick. So I think it would be safe to include that in the modeling that you would use going forward.

Operator

And our next question is from Stanley Elliott with Stifel.

Stanley S. Elliott - *Stifel, Nicolaus & Company, Incorporated, Research Division - VP and Analyst*

Quick question on that SG&A piece. We're not see -- the $10 million is just what you all have done from a cost restructuring perspective, and that does not include lower legal expenses. Is that correct? And when would the lower legal expenses start to flow through, too?

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

Yes. That's correct. And as I talked about, Stanley, on my prepared comments, we had talked about $3 million higher of certain costs. A part of that is the legal cost that we've incurred in our insurance recovery program. It's really hard for us to say when those costs will come down. What we would say is that we're making really good progress at securing payment in the insurance arena. But in terms of providing guidance on legal cost coming down, that's challenging in where we sit currently in this environment.

Stanley S. Elliott - *Stifel, Nicolaus & Company, Incorporated, Research Division - VP and Analyst*

That's fine. And as far as the new fixed gas products, when can you guys start shipping those? Is that what was driving the big backlog increase in the Middle East? Just curious to what you guys could say about that.

William M. Lambert - *MSA Safety Incorporated - Chairman, CEO and President*

Yes, I assume you're referring to the new X5000 and S5000 products that we launched this week. Those products are already shipping, Stanley. So when we launch those this week, we were immediately shipping certain back order that we had built up in that area. To answer your second part of your question, no, I would not say that those, that large back order that we're building up and solid order pace that we're seeing in the Middle East, is because of these new gas detectors, the X5000 or S5000. I think that's more base business in some of the existing product line, but I will say that our sales reorganizations are really excited about this next generation of product. And as we are now ramping up into full production, I would expect to see that have a greater and greater impact over time.

Stanley S. Elliott - *Stifel, Nicolaus & Company, Incorporated, Research Division - VP and Analyst*

Perfect. And then on the margin piece in North America, you mentioned that kind of the SCBA was a big driver. Does that include the ability to ship the new thermal imaging camera in the handpiece? Or is it just you guys have gotten better in terms of sourcing and throughput and just the general blocking and tackling, if you will?

William M. Lambert - *MSA Safety Incorporated - Chairman, CEO and President*

Well, I think it's a bit of both of the items that you discussed and also better blocking and tackling. Ken mentioned in his comments improvements in productivity that we are seeing. Americas operating margin was around 23%, as I remember, up above over 400 basis points over the prior year, which was terrific to see. And some of that is driven by the new iTIC that is shipping with SCBA that's allowing us to garner a much higher average selling price for the SCBA that we're selling. It's the kits that we're sending out where we have the ability to now upgrade the G1 SCBA that have been sold over the past 2 years and include the iTIC to that, as well as just improved vendor relations, supply chain management activities and productivity on the factory floor. So we're seeing the benefit of all of those measures, I don't have -- I can't parse it for you, but maybe in the future, we can give you a better sense there of what's happening.

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

The only thing I would add to that is on the gross margin line from a consolidated perspective, we did see a nice performance with 180 basis points of improvement. About 40 basis points or so of that improvement is mix. About a 100 basis points of that is the SCBA, but we did see meaningful improvement across all of the core. And so we -- it was a good quarter with respect to margin performance.

Stanley S. Elliott - *Stifel, Nicolaus & Company, Incorporated, Research Division - VP and Analyst*

No doubt. And then lastly in terms of M&A or potential to grow the business in other avenues, you obviously have a lot of financial flexibility, capacity. But kind of what's the market looking like right now? There's been some larger deals that have happened in this space. Has that pushed up multiples? Pushed up expectations? Kind of changed your thought process on when and where and how to proceed with deals? Any color there would be great.

William M. Lambert - *MSA Safety Incorporated - Chairman, CEO and President*

Well, I think during this past quarter, you saw a recent very strategic acquisition made by one of our competitors. And as you noted, our balance sheet is in a very strong position. I'll tell you that we continually review the acquisition pipeline in our -- in many of our core areas, and we evaluate how certain targets could add value to MSA. And we continue that process and we remain focused on that area. We look at opportunities across our core areas and our core end markets. And you can see that from the strategic transaction costs that we incurred in the quarter, we're actively looking at opportunities to find the right investments that are going to grow our business. So I think it's safe to say that we can and we will use our additional debt capacity and improved cash flow, first and foremost, to grow the business. And part of that is looking very closely at -- and carefully at acquisitions in this space. Multiples are higher, I think, in this space than generally seen in the industrial space, and so that becomes a factor.

Operator

And our next call -- or question is coming in from Edward Marshall from Sidoti & Company.

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

So you've already kind of made the comments on the comparable from fall protection equipment in the quarter. I was curious, as I parse through the different -- Americas versus the international business, obviously, the weakness was in international. I'm wondering if there's also some seasonality that you didn't see last year in that business that might have flown through in the first quarter. And then secondarily, I think after a year after integration, I'm wondering about the cross-pollination of your products, your brand and the technologies. And is any of that playing off into the Americas division as well?

William M. Lambert - *MSA Safety Incorporated - Chairman, CEO and President*

Yes. I'll address the last part of that question first, Ed. We are absolutely seeing nice cross-pollination of the Latchways acquisition into the Americas. In fact, the Americas saw a 13% increase in fall protection in the first quarter versus a year ago. So we're seeing a lot of that cross-pollination that we had hoped to see, and gaining strides there and seeing a nice uptake in our market share performance in the Americas. International was down quite considerably in fall protection, I think down 21% or in that range. A lot of that was related to some large orders and backlog that we had in the U.K., and it was all Latchways product. So we just went over -- were able to overcome some of that, but I don't think that, that in any way throws cold water on our optimism for this product line in Europe. And we've got some exciting new products planned for this year in Europe. And we expect to see some continued strong growth across our fall protection line. Maybe not 20 plus percent like we were able to see last year, but we still have good, solid expectations for fall protection in this business.

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

Got it. And you mentioned the thermal imaging cameras design for the G1 and works well with that system, battery packs, et cetera. I'm assuming it also works with older generation equipment. Just wanted to be clear.

William M. Lambert - *MSA Safety Incorporated - Chairman, CEO and President*

No, Ed, it does not. It only works with the G1 SCBA.

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

Got it. And then the acquisition in this space that we've talked about or hinted to, I'm kind of curious how you see that development around the SCBA product in particular. Do you think it helps or hurts your continued market share gains in the -- with the new G1 and the thermal imaging camera?

William M. Lambert - *MSA Safety Incorporated - Chairman, CEO and President*

Well, I think that the -- our experience in developing the G1 was that it took a very significant amount of investment and took us 5 years to bring that to market with the amount of voice of customer research that we did in order to hit the bull's eye the way we did. I think that the G1 has now been on the market and been sold into the market for 2 years. So certainly, the competitive landscape has had an opportunity to look at the G1 and to identify the great features of it and features that they think they could improve upon. But we continue to innovate around the G1. The iTIC is the latest, most visible example, but we have other activities in process here to build off of that platform. It's just not a standalone product the way previous generations of SCBA have been. This is a product that we are viewing as a platform for the fire service that integrates various activities, including communication and thermal imaging, vision capability, as well as other integration capability with, say, gas detection instruments and firefighter location capabilities that can come in the future. And I think it becomes a challenging target for our competitors, and that makes us feel pretty good. But we're not at all sitting still and taking great comfort in it. There's still a lot of work to do and there's still a lot of market share to be gained.

Operator

And our next questions come from Brian Rafn from Morgan Dempsey Capital Management.

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

Yes. Hello. Can you hear me?

Operator

Yes, we can now.

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

Sorry guys, I'm on the road, I'm on a cell phone. Can you guys hear me at all?

William M. Lambert - *MSA Safety Incorporated - Chairman, CEO and President*

Yes, Brian, we can hear you.

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

Okay. Yes. I just wanted to ask Bill. As you look at -- you talked about the SCBA, the G1, the new platform. You guys have certainly bought a major amount of technology. You have constant iteration, updates. And as you look at the lifespan of that G1, does that affect the next generation, where you might keep the G1 as a [dual] product? And if you have a 10- or 12-year lifespan at this product, does -- at some point, you guys suspend new technology iterations to go to the next generation?

William M. Lambert - *MSA Safety Incorporated - Chairman, CEO and President*

Well, I think that if, I heard your question completely, Brian, we look at the G1 SCBA as a platform that we can drive at least 15 years, 10 to 15 years of life out of. With all the software enhancements that can be made to that product and some of the integration capability that, that platform provides us, we think that can be extended somewhat. The fire service is a very, very demanding environment. And so it's not as simple as bringing new technology to the fire service market as it might be bringing new technology to the consumer market. And iterations of smartphones may be very, very fast. But for the fire service, that iteration is not as fast. And it requires a lot of market research and understanding of what happens on the fire ground. And I think the G1 represents the very best of technology that's available today. And the path that we are following is to add to that platform with technologies that I talked about with the previous caller. And that should give us, I think, a 10- to 15-year runaway for this product line, which we just introduced 2 years ago.

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

Okay, I appreciate the color, Bill. With the complete (inaudible) technology in that G1 platform, do you assume that it's going to be (inaudible) [landing trial] with the fire service regulators that you'd factor -- I think there was some delays. And do you guys think that, that's probably, going forward, that type of evaluation is going to be more of a drawn out affair?

William M. Lambert - *MSA Safety Incorporated - Chairman, CEO and President*

Yes, again, Brian, it is a little bit difficult to hear you. But what I think you were asking had to do with getting it through the regulations and the approval agencies. And do I see that as getting any worse or getting any better? I don't think it's changed much, it's still a challenge to get it through government approval agencies. The time constraints there continue to be challenging. But it's not getting any worse is the good news. Let me put it that way.

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

Okay. And then one final question maybe for Ken. Ken, what -- from standpoint of M&A, what kind of deal size would you guys be looking at, given your balance sheet strength?

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

So if I understand it correctly, I think you're asking around deal size and capital allocation. And what we've done historically is we've certainly have used our balance sheet. We've put our balance sheet to work. For the General Monitors acquisition we made several years ago, I think we levered up between 3.5x and 4x. Recently -- more recently with Latchways, we were between 2x and 3x. So we certainly have the capacity and the capability to follow what we've done in the past and use our balance sheet and put it to work in order to find growth opportunities.

Operator

And our next caller is Richard Eastman with Robert W. Baird.

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

I just wanted to double back. Bill, in your commentary around the core product revenue performance in Q1, it strikes me that the soft spots, fall protection, FGFD and then SCBA, you did comment that the order performance in all 3 of those categories, as well as I think you suggested the backlog, was up at the end of the first quarter. Is that the right take here? And also, is that where you get your confidence that even if we started with this core products down 3% in the first quarter that we're still comfortable with this low single to mid-single? Do I -- did I put the pieces together properly here?

William M. Lambert - *MSA Safety Incorporated - Chairman, CEO and President*

Yes, I think you did, Rick.

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

Just adding -- here's texture there, Rick. Just adding some texture there, Rick. I mean, on the fall protection side, I know we called out head protection and portable gas growing, order growth of 24% and 19%, respectively. Well, fall protection also. And we saw 10% order growth in the quarter. So we built a little backlog in the fall protection area. The fixed gas and flame detection is coming in right around where we thought it would. So it's hitting our plans. And the SCBA, as Bill talked about in his prepared comments, the order flow was certainly good for us. And so yes, I think we're positioned well to continue to track towards that guidance that we had previously issued.

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

It was the F -- the fixed gas and flame business, was there any impact from the impending introduction of the X5000 and S5000? I mean, just any reluctance to order, I won't say old, product. But did that impact either international or domestic sales for FGFD?

William M. Lambert - *MSA Safety Incorporated - Chairman, CEO and President*

Rick, it's hard to put a firm number on it. But the sense is it does. We've talked about X5000 and S5000 now for at least the past 2 quarters. And we also talked about some of the challenges in getting it through the approval agencies and getting the product launched and shipping. We finally overcame those. But I think the amount of enthusiasm that we built up with that product line undoubtedly has a bit of an impact where rep organizations that sell our product, and our sales force, tends to be looking toward this next generation of product, and maybe they're a little bit more hesitant. But for us to put a -- for me to give you a firm number, I really can't do that. But it's my belief that, that does have an adverse impact.

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

Yes, okay. And then just last question. This past month or so, Grainger took some -- announced some very aggressive pricing actions to enhance its competitive position against, I think, Amazon in this -- in the industrial distribution area. Is there any reason to be concerned that what Grainger is doing on the pricing side may get pushed back to the vendors that use Grainger as a channel, meaning MSA?

William M. Lambert - *MSA Safety Incorporated - Chairman, CEO and President*

Well, yes. The short answer is yes. There is always that risk. Grainger is very aggressive in pricing negotiations with us, but we also have relationships with Amazon and Fastenal and other major industrial distributors to secure that -- those channels of distribution. So I would say yes, it's always a concern. Pricing negotiations are always tough. But with some of the improvements we've seen in gross margin and the offsets in costs and improvements in productivity, we've been able to weather that storm to this point in time.

Operator

Now back to Mark for further remarks.

Mark Deasy - *MSA Safety Incorporated - Director of Corporate Communications*

Thank you, Jamie. Seeing that we have no more questions that will conclude today's call. And I just want to remind everybody that if you missed a portion of the call, a replay and a transcript will be available on our website for the next 90 days.

So on behalf of Bill and Ken, I want to thank you again for joining us this morning and we look forward to talking with you again soon. Have a good day.
