BUILDERS FIRST SOURCE

Moderator: Floyd Sherman
October 24, 2014
10:00 am CT

Operator: Please stand-by, we're about to begin. Good morning and welcome to the Builders First Source third-quarter 2014 earnings conference call. Your host for today's call is Mr. Floyd Sherman, Chief Executive Officer.

At this time all participants are in a listen-only mode. Later we will conduct a question and answer session and instructions will follow at that time. Any reproduction of this call in whole or in part is not permitted without prior written authorization of Builders First Source.

And as a reminder, this conference call is being recorded today, October 24, 2014. The company issued a press release after the market closed yesterday. If you don't have a copy, you can find it on our Website at brdl.com.

Before we begin, I would like to remind you that during the course of this conference call management may make statements concerning the company's future prospects, financial results and business strategies and industry trends. Such statements are considered forward-looking statements under the Private Securities Litigation Reform Act of 1995 and are subject to certain risks and uncertainties which could cause an actual result to differ materially from expectations. Please refer to the most recent form K-10 filed with the Securities and Exchange Commission and other reports files with the SEC for more information on those kinds of risks.

The company undertakes no obligation to publicly update or revise any forward-looking statements. We have provided reconciliations of non-GAAP financial measures to their GAAP equivalents in our earnings press release and detailed explanations of non-GAAP financial measures in our form 8-K filed yesterday both of which are available on our Web site.

At this time I would like to turn the conference over to Floyd Sherman. Please go ahead, Sir.

Floyd Sherman: Thank you and good morning. Welcome to our third-quarter 2014 earnings call. Joining me today from our management team is Chad Crow, Senior Vice President/Chief Financial Officer and Marcie Hyder, Vice President and Controller.

I'll start with an overview of the third-quarter. I'll then turn the call over to Chad who will discuss our financial results in more detail. After my closing comments regarding outlook, we'll take your questions.

We ended the third-quarter of 2014 with sales of approximately $435 million and on a same store basis, increased our sales by 5.3% compared to the third-quarter of 2013. Our sales volume excluding the impact of recent acquisitions grew 6.6% before a 1.3% negative impact of commodity priced deflation on sales.

For the current quarter, the U.S. Census Bureau reported actual single family housing starts in the south region which encompasses all of our markets increased 10.5% compared to the third-quarter of 2013. On a September year-to-date basis, actual single family starts increased 4% in the south region compared to 2013 while our sales volume grew 9.9% before a 3.1% negative impact of commodity priced deflation on our sales.

In addition to our focus on profitable organic growth, our focus has also been on growing through acquisitions. Our recent acquisitions in the Orlando, Houston, Dallas and Austin markets should allow us the opportunity to expand our product and service offerings to a more diverse customer base in what we consider very attractive housing markets.

On a trailing 12 month basis as of their respective acquisition dates, these recently acquired companies had generated combined revenues of approximately $67 million. I'll now turn the call over to Chad who will review our financial results in more detail.

Chad Crow: Thank you Floyd. Good morning everyone. For the current quarter, we reported sales of 434.9 million compared to 402.9 million for the third-quarter of 2013, an increase of 32 million or 7.9%. Excluding the impact of recent acquisitions, we estimate sales increased approximately 6.6% due to increased sales volume which was offset 1.3% by the impact of commodity priced deflation on our sales.

Looking at our sales by product category, prefabricated components were 90.2 million, up 8.8% from $83.0 million in the third-quarter of 2013. Windows and doors were 97.7 million, up 15.8% from 84.4 million last year. Lumber and lumber sheet goods were 141.7 million, up 3%. Our millwork category was 42.7million, up approximately 14% and other building products and services were 62.6 million, up 3.4% from last year.

From a product mix standpoint, our value add product categories made up a higher percentage of overall sales while lumber and lumber and sheet goods and other building product and services declined as a percentage of total sales. I will also point out that revenue related to installed material and labor fell almost 5% compared to the third-quarter of last year. This is representative of our willingness to want business when pricing is not acceptable especially in the area of installed services.

Our gross margin percentage was 22.5% in the current quarter, down from 23% last year largely due to more favorable trends and market prices for commodity lumber and lumber sheet good products in the third-quarter of last year. Our gross margin percentage has shown continual improvement this year and is up 90 basis points on a year-to-date basis.

For the current quarter our selling general administrative expenses increased 9.6 million or 13.3%. Excluding the impact of recent acquisitions SG&A increased 7.5 million of which approximately 3.3 million was attributable to higher sales volumes. The remaining 4.2 million that I would like to label as an unfavorable flex in our operating expenses, consisted of 1.1 million of additional group health expense – we are self-insured up to 3 hundred thousand per claim and have had an unusually number of high claims hit us in the back half of this year.

We also had 1 million of incremental non-cash stock comp expense related to equity grants earlier this year. Going forward our quarterly stock comp expense will be consistent with the 2 million expense in the current quarter. While this is one of the add-backs to adjusted EBITDA, it will be reflected as incremental SG&A on our P&L.

We also had approximately 1.6 million of incremental expense I would classify as infrastructure investments that were made in anticipation of stronger housing starts this year. Specifically an additional 6 hundred thousand in lease expenses on delivery equipment and approximately $1 million in incremental personnel costs largely related to hiring and retaining truck drivers.

I want to give you a little more color on this. We had budget single family starts this year to be up approximately 18% from last year which at the time was below other industry estimates that average around a 25% increase, so more than we had budgeted for.

So you're left with the choice. Do we strip things down again in response to slower growth knowing that we may be left short on equipment personnel when things pick-up or do we hold onto some of the incremental investments made in anticipation of stronger growth?

Well, we are doing a little of both but the bottom line is our money says housing will continue to get better over the next couple of years not worse so we may be a little heavier in some areas than we need to be over the next couple of quarters in anticipation of this growth but we will continue to weigh the risk/reward of reducing these costs and will make adjustments as we deem necessary.

As an example, as of today we are currently having to decide what we need as far as equipment for next year. For example, a truck ordered today will not be received until March or April of next year, so there is some lead time in preparing for growth in the business. Our SG&A expenses expressed as a percentage of sales were 18.8% compared to 18% in the third-quarter of 2013. The incremental unfavorable expenses I outlined increased our SG&A expense as a percentage of sales approximately 90 basis points in the current quarter.

Interest expense was 6.4 million, a decrease of 1.1 million. The decrease was primarily related to 1.1 million reduction in the non-cash fair value of stock warrants issued in connection with our 2011 term loan.

We recorded 5 hundred thousand of income tax expense compared to a hundred thousand income tax benefit in the third-quarter of 2013. We recorded a reduction of the after-tax, non-cash valuation allowance on our net deferred tax assets of 3.3 million and 3.4 million in the third quarters of 2014 and 2013, respectively. Absent the valuation allowance, the effective tax rate exclusive of the discrete items would have been 40.7% and 25.8% in the third-quarter so '14 and '13 respectively.

As of September 30, our gross federal income tax net operating loss available for carry-forward was approximately 247 million. Income from continuing operations was 8.7 million or 7 cents per diluted share compared to 13 million or 13 cents per diluted share in the third-quarter of 2013. Our adjusted EBITDA was 20.2 million or 4.7% of sales for the current quarter compared to 23 million or 5.7% of sales in the third-quarter of 2013.

We ended the current quarter with total liquidity of 197 million consisting of 67.8 million of cash and 129.4 million in borrowing availability on a revolving credit facility. In July 2014 we borrowed 30 million under our senior revolving credit facility and still have 30 million outstanding as of the end of September.

Operating cash flow was 29.8 million for the third-quarter of 2014 compared to 29.7 million last year. During the third-quarter of 2014, we used approximately 24.4 million of cash on hand to acquire West Orange Lumber Company and Truss Rite LLC. On October 1 we used approximately 19.4 million to acquire Trim Tech of Austin.

Capital expenditure were 2.4 million for the third-quarter of 2014 compared to 4.8 million for the same quarter of 2013. Capital expenditures in the fourth-quarter of 2014 are expected to approximate 10 million, most of which is related to the relocation of an existing facility and the opening of a new facility, both in the state of Texas.

I'll now turn the call back over to Floyd for his closing comments.

Floyd Sherman: Thank you Chad. We continue to believe the long-term outlook for the housing industry remains positive and at the pace of the recovery will accelerate as consumers gain more confidence in the economy and pent-up housing demand gets released.

We will continue looking for ways to improve our profitability while still growing our market share including seeking additional strategic acquisition targets in order to have even better positioning, in order to be even better positioned for such a rebound.

I'll now turn the call over the Operator for Q&A.

Operator: Thank you. Today's question and answer session will be conducted electronically. If you would like to ask a question at this time, please press star 1 on your touch-tone telephone. If you're using a speakerphone, please turn your speaker function off to allow your signal to reach our equipment. Once again, that is star 1 if you have a question at this time.

It appears our first question comes from John Baugh with Stifel.

John Baugh: Thank you and good morning Floyd and Chad. I wanted to probe on the acquisitions. You mentioned expand customer base. What are you really getting both financially and strategically through the acquisitions? And I guess what I'm trying to get at is it simply just getting larger in good markets at an attractive financial or is there something specific about any of these companies that brings management or product lines or some kind of expertise? Thank you.

Floyd Sherman: Well I think John, when you look at the acquisitions that we've made with the Truss Manufacturing Companies, those companies will enable us to become more involved with the multi-family sector of the business. That's where their primary focus is on. We think the multi-family business will continue to be very good. It looks like multi-family construction over the next several years will be more robust than single family.

These operations will certainly allow us to gain better penetration into that particular market and in the areas that, where we acquired the plant. And so we look at that strategically as being very, very important to this company to do, get into, more involve in the multi-family.

We like the multi-family business where we can deliver a product without getting involved in a lot of install work. We like (trusses). We also like the millwork category and those areas in particular are of real interest to us.

The, we also really wanted to be able to get into the Houston market. We think the Houston market can be really expanded. We are involved - at the current time, up until the acquisition, the only products we sold in the market were windows that are manufactured at our Houston, Texas plant.

The particular acquisition that we did in Houston will enable us to really expand our presence. We think that this will be a very, very large market for us going forward and the, this acquisition gives us a chance to enter the market with a company that had excellent reputation, very high quality people, were well established in the market.

And, in fact, we've already acquired another facility to enlarge that company's operations within the Houston market. So we see the Houston market as a long-term major market to participate in.

The acquisition that we did in Orlando, that gave us not only building products distribution but it also enabled us to get into a commercial door arena which we have not participated in at all and as well as with the Truss manufacturing operation.

So that we're not only increasing our exposure to the Orlando market with traditional building products but also opening up added venues for us with roof trusses and commercial door products.

So I think that pretty much sums up what we've done so far and this is what we're going to continue to look for. We want to add more manufacturing content to the company. We want to add more value, added products and we think that that in the long term is what will produce a better earnings stream for us.

Chad Crow: And I'll just add, I'll just add on the Trintech acquisition certainly gives us deeper penetration into a, in a strong market in Austin but it also gives us a lot more exposure to some high-end custom builders and also comes with a highly experienced management team as well.

John Baugh: And I appreciate that color. I'll get into modeling details with you later Chad but how do we think about these 67 million of revenues and what you paid? How do we think about that in total financially for the next 12 months or so?

Chad Crow: You know, obviously the plan is to grow these businesses and expand their value-add content. They are certainly very high EBITDA margin, acquisitions as well. So I think there's a lot of good opportunity there. We can, like you said, we can talk more specifics later, if you like.

John Baugh: Okay, and my follow-up question is just on the housing start number. You commented that year-to-date, it's up 4% in your area. Latest quarter though was up 10 and of course your revenue are a little bit lagged through all that. Should we take this to mean that the revenue may accelerate with the recent quarter's strength in single family, Floyd?

Floyd Sherman: Yes, we've definitely got the starts in our area but keep in mind there is a lag from the time a start is taken out and until the actual construction process begins. That could be 60 to 90 day so we think that this will, should produce stronger results for us looking forward.

But as I look at the fourth-quarter, I think the fourth-quarter of this year is going to resemble a lot like our third-quarter. We had indicated on the last call, we thought the third-quarter was going to look very much like the second-quarter and I think we were very much spot on.

As it turned out the, I, as Chad said, we do feel and looking forward to next year, I think in our projections were are anticipating low double-digit growth in housing. That's what right now we're building our budgets around. I know there's some higher numbers. Some lower numbers but our feeling is that housing is continuing to improve, continuing to strengthen.

Certainly some of the actions that have been and the conversations that have come out of the Federal Housing Finance Agency as it relates to loosening rules on mortgages, certainly is positive for us. I think it will start helping bring back the first time home buyer into the market.

So we're feeling better as we look forward in the business and I think the fourth-quarter is business wise, trend wise, I think it's going to have a lot of similarities to what we've seen in the third-quarter. Chad, you may...

Chad Crow: Yes, well obviously there's some seasonality affecting Q4. I think last year from Q3 to Q4, our sales dropped about 8% due to that seasonality effect. Probably see a similar drop this year, Q3 to Q4. I think our gross margins should hang in there pretty close to where they were in the third-quarter of this year.

We will be a little heavier as I discussed earlier on the operating expense side so I would expect our Q4 EBITDA to come in pretty close to where we were in Q4 of last year.

John Baugh: Thank you. Good luck.

Chad Crow: Thanks John.

Operator: Our next question comes from Philip Volpicelli with Deutsche Bank.

Philip Volpicelli: Good morning.

Male: Morning Phil

Philip Volpicelli: Chad, unfortunately when you were talking about the items that caused the SG&A to be up, unfortunately my line cut out. Could you just go over those once again and then could you talk a little bit about how we should think about SG&A for 2015? Is it best to think about it as a percent of revenue or is it best to think about it as a fixed versus variable and, you know, how should those components change?

Chad Crow: Sure. Excluding the impact of acquisitions in the third-quarter our SG&A increased about 7.5 million of which about 3.3 million was attributable to higher sales volume which again, we said in the past our OPEX would be 65 to70% variable to increases in sales volume so that's consistent with what we said.

But on top of that we had just over 4 million of what I would consider unfavorable flags, 1.1 of that was some unexpected group health expense cost. We've had quite a rash of higher dollar claims this year. We're probably on pace this year to be at least, have two to two-and-a-half as many, what we call higher dollar claims over $50 thousand.

So that was an incremental 1.1 million in the quarter. We had the 1 million of incremental stock comp expense. That's non cash. It's obviously an add-back of our EBITDA but it does increase operating expense on the P&L.

And then we had another 1.6 or so that I was saying were more infrastructure type investments, investments in delivery equipment. Six hundred thousand of that 1.6 million is incremental lease expense on delivery equipment and then about another million of incremental personnel costs in investments we had made in personnel in anticipation of the higher growth largely in the area of delivery and retaining qualified drivers.

So that's the bulk of the change in the operating expense so some of this to a degree is an investment on future growth. I still think long-term our OPEX is going to trend very well with growth in sales and I would probably, you can look at it both ways.

I think you can look at it 65 to 70% variable to volume growth which obviously should drive down our OPEX as a percentage of sales in future years.

Philip Volpicelli: Okay, that's very helpful. Thank you. And when you look about, in your regions now clearly the third-quarter starts were up much better than what you've seen in the first six months of the year.

What's the tone that you're getting from your builder customers now?

Male: Say that again. You were breaking-up, Philip.

Philip Volpicelli: Sorry about that. Can you hear me better now?

Male: Yes.

Philip Volpicelli: I was just wondering what the tone is from your builder customers now in the southern region now in terms of starts because you had a weak start to the year, a pretty good third-quarter at 10.5% increase. Are you feeling that momentum continue?

Male: Yes, I definitely feel the momentum is continuing. We, the builders are feeling very confident. We're getting, we continue to get, you know, very encouraging reports from our builder customers. I think the, their outlook going into next year is certainly a lot better than what we saw earlier in the year, a lot more positive and I think it's going to reflect in a continually improving housing market.

We, you know, even coming off of a year that looks like it's going to be for the year a relatively flat, very, about a 5% growth on starts where next year we're rally saying it's going to be somewhere in that 10%, you know, give or take a point or two and that's the way we're budgeting. And that's largely based on the feelings that we're getting from our customers and the confidence that they're showing as they look to next year' building plans.

Philip Volpicelli: Okay great. Two questions on acquisitions and then I'll pass it on. What were the EBITDA contributions from the four acquisitions you completed? And what's your appetite for the rest of the year in terms of how much more you might consider spending?

Chad Crow: We're not going to disclose the EBITDA contribution on those. I think as Floyd laid out earlier, we are, we do certainly have an appetite to go after some additional companies, especially those with a high mix of value-add products.

Philip Volpicelli: Okay, great. Thank you very much. Best of luck.

Chad Crow: Next.

Operator: Our next question comes from Lee Brading with Wells Fargo.

(Melissa McQuire): Yes, hi actually this is (Melissa McQuire) in for Lee Brading. Thanks for taking the question. We were looking at another good quarter of growth in your pre-fab business and was hopping you can discuss its impact on market share. It looks like it went down a percentage of total mix a little from Q2 but was hoping to get any color you have on flow through from that business into any of your other product lines.

Chad Crow: The demand for those products is still certainly strong and we anticipate that that demand will continue to grow. We did have a very strong quarter when you look at the windows and door category and sometimes when you see some growth in one category that kind of outpaces others, it obviously pushes the others down as a percentage of total but the growth in that category is still very strong.

(Melissa McGuire): Great and then, was curious, is that growth driving increase in share volume with your increasing customers. I think you mentioned in the past maybe getting in the door on a free prefab side and then expanding outward to other lines.

Chad Crow: Well to the extent that starts haven't been what we had hoped this year, the additional penetration on that product line with some customers hasn't played out like we had hoped but I think as long as we continue to see an increase in starts that's when the demand for that product category will continue to accelerate so I fully expect as starts grow, there will be higher demand for that product and more penetration with existing customers.

(Melissa McQuire): Got it. Thanks. And then you just mentioned the strength in the windows and doors category. I know some of the other window and door manufacturers have been announcing price increases. Is that driving a lot of the sales growth you guys are seeing or what's, give me some color and magnitude of pricing benefit versus volume increases.

Chad Crow: Well it's both. Certainly price increase as long as we're able to pass those along can help the topline in those categories. So that is part of it. Part of it is also our, as Floyd mentioned, we have a window plant in Houston and that plant continues to perform really well and continues to take share down there.

So it's a combination of both. I don't' have any more of a breakdown on that for you.

(Melissa McQuire): Okay, great. Thanks a lot.

Chad Crow: You bet.

Operator: Our next question comes from Seth Yeager with Jefferies.

Seth Yeager: Hey, good morning.

Male: Hey Seth.

Male: Morning Seth.

Seth Yeager: Hey, I don't know if it was just me but just as a head-up, at least at the beginning of the call it was cutting-out quite a bit. Can you, I respect you're not giving specific margins or multiples in the acquisition. Can you maybe talk about the percentage of mix, like what's commodity versus value-add roughly. I apologize if I missed that before.

Male: Well certainly they have a high percentage of value-add, just trying to add it up here in my head, I would probably say it's 60 to 70% value-add versus distribution.

Seth Yeager: Okay, no, that's helpful. And the multi-family exposure that you had mentioned, what sort of risk does that look like with the recent additions?

Male: Well, the multi-family's going to be almost 100% value add. That's primarily supplying roof trusses and floor trusses.

Seth Yeager: Got it. Okay, that's helpful. And is there anything you can share around how you position your inventories going into the quarter. I think it's about $10 million on a, on a, it gets, versus the priority year. How much of that was from the acquisitions versus any strategic purchases you guys may have made?

Male: I would say probably the bulk of it is due to the acquisitions, you know, commodity prices have been pretty flat this year. We really don't expect to see a whole lot of movement in them and so while we may have taken advantage of a few opportunities on the buy side, I think most of that's going to be the acquisitions.

Seth Yeager: Got it. Okay and the additional group health expense, is that going to be run-rated going forward or is that more of like a onetime item during the quarter?

Male: Well I do think we have some more larger claims that have yet to come through in the back-half of the year but no, I don't think it's going to be a run-rate from here on. Hopefully when we get past his wave we're seeing in Q4 that we'll see that settle down a little bit.

Seth Yeager: Okay and then last one for me. In terms of cash flows, how are you prioritizing? You obviously mentioned some acquisitions, are there still some moth ball facilities that you can bring back online that are maybe a little more accretive? And how quickly do you anticipate the borrowings under the ABL?

Male: Well we do have one or two facilities that are still mothballed. Right now the demand in those particular markets just does not re-justify reopening those, so I really don't see that happening in the next quarter or two. As far as the revolver goes, yes we'll pay it down as soon as we can but a lot of that will depend on if we're able to come across any attractive acquisitions in the meantime.

Seth Yeager: Okay, all right. Best of luck. Thanks.

Operator: Our next question comes from Justin Bergner with Gabelli & Company.

Justin Bergner: Good morning Floyd. Good morning Chad.

Male: Morning Justin.

Justin Bergner: I just wanted to start and understand the dynamics of the market a bit better. Has anything sort of meaningfully changed over the last three months in terms of, you know, labor, availability or competitive behavior in the housing market as it relates the powers you supply and I guess I'm also wondering about the decision to exit certain business which might have been attractive a couple of months ago?

Floyd Sherman: We're not exiting certain businesses but just sort of pull back from, you know, certain installation business. Well the labor situation still remains very tight. The, that's the entire construction industry and it's not just limited to our sales is still, you know, the very tough feeling of finding the skilled labor that's required and also being able to control the costs of that labor.

The, but it's not getting any worse. It hasn't gotten any better but it still is a major issue that we have to deal with. So I can't really say that the labor is a deteriorating situation for us and so I guess we're all leaning to live with it and we're taking care of the business that we have to take care of.

I really don't believe at this point that it's holding back construction. There may be some occasional delays that you're running into but that's about the extent of it. Chad, you have any other color?

Chad Crow: No, that's right. It's still, it's still pretty tough from the labor standpoint. You know the decision to exit some of the installations, or anytime you install something you're taking on a little bit of additional risk and we need to be paid for that risk.

And so there are situations out there where we don't feel like we are getting paid for that risk and that's why we made the decision to reassess whether we do some of that business or not.

Male: Yes and I think that when you look at what took place in our business third-quarter this year compared to the same period last year. When you look at the important segments of our business, the value-added segments of our business, prefab components were up almost 9%, window and door up almost 16%, millwork up about 14%.

They were really major increases and that was offset by only a 3% gain in lumber sheet goods and about 3.4% for the other building products and services which were heavily weighted towards install. We put a lot of focus on increasing our efforts where we could get better margins, circling in the areas of the lumber, lumber sheet goods, extremely price competitive.

We recognize we've got to do this. This is still an important part of the business but we're willing to walk from a business where we can't get what we think is fair pricing for our services and the products that we supply to the job site. The same thing holds true for install.

If we don't feel we can get the margins, the pricing that justifies the risk that we have to take on, then we're going to pass on some of that business and we'll wait until conditions improve. We're not exiting from the business. We're just redeploying some of our effort in a direction that will give us a better positive result.

So I feel really good about the gains that we made in the value-add sectors of our business. If you look at those, we had double-digit increases and what brought our overall, the sales gains down, was we backed off of and we walked from a lot of dollars of business in the commodity area of the business as well as on the install side where we just didn't feel that there was a reason to pursue it.

Justin Bergner: Great. Thank you for that color. I had one other question which is the 1.6 million of SG&A that was sort of defined as infrastructure spending. Is that spending that was put into place in Q3 in anticipation of sort of a second-half pick-up, I mean given that it didn't hit prior quarters?

Male: No it was in place in Q2 as well.

(Crosstalk)

Floyd Sherman: It was bleeding in in Q2 and continued to come in in Q3 especially on the equipment side but some of that equipment is trickling in as the year goes on because like I said earlier we'd ordered that stuff six months ago.

And on the wage side of it, especially as it relates to drivers salary, Chad, we had major increase that we had that we would pay out to the hard drivers salaries in order to keep, in order to keep our driver. As you know, there's a major shortage of CDL drivers in this country.

Every trucking operation is open to pirating from the competitors and drivers are absolutely essential for us and the skills that's required when you're delivering building materials to a job site and having to place materials on a job site is far more difficult and takes a lot longer for people to get those skills than it is just driving point A to point B which many of the over-the-road drivers, you know, have to do in their job.

So we really have been concerned with being able to hold onto our drivers and our ((inaudible)) because that's going to determine to a great extent your ability to take advantage of an expanding housing market as we go forward. Just as a salesman is important, those driver are absolutely critical to us in getting the materials to the job site and maintaining our service to the customers.

So the driver's salaries, increases were very much unexpected and this has been something that really started accelerating. We started seeing a little bit of it in the second quarter and it really developed during the third-quarter in particular.

Justin Bergner: Okay. Thanks for that detail. So when I think about sort of the SG&A spend sequentially third-quarter versus second-quarter, that 1.6 million wasn't so much of a step-up sequentially. It was more the other factors that you talked about?

Male: That's right.

Justin Bergner: Okay.

Male: It was primarily, it was primarily the stock comp and the group health.

Justin Bergner: Okay, well thank you. Good luck the rest of the year.

Male: Thank you.

Operator: And just as a reminder, please press star 1 if you have a question at this time. Our next question comes from Sam McGovern with Credit Suisse.

Sam McGovern: Hey guys. Thanks for taking the question.

Male: Hi Sam.

Sam McGovern: Again I may have missed this given the phone difficulties earlier, but in terms of the pricing pressure that you guys have seen from some of your smaller private competitors, obviously that's driving from excess capacity, what do you think it takes to really get that out of the system, just a pick-up in demand that will eventually sort of take care of that or is it just sort of waiting guys out until they sort of dry up from liquidity and they have to exit the market.

What gets you to a point where there's a little bit more balance in terms of supply and demand?

Floyd Sherman: I think it's really a combination of both of those things. Very definitely, you know, Sam, this year was a year, we entered the year with very high expectations and I think so did the rest of our competitors. Everyone was anticipating a much more robust housing market.

You know, people put in CAPEX, expanded their business, increased the supply and then unfortunately the market hasn't developed to anywhere close to anyone's expectations. So there still is a lot of supply chasing the demand.

As we move into more, as the housing continues to move up, that begins to eat up. I think people are going to be less anxious to get out in front of themselves similar to what we did here in this company.

Going forward, I think that there are a lot of competitors that are really experiencing issue with getting the necessary working capital to expand their business, take care of properly servicing their customers. And so I do believe that we're going to continue to see people fall out and pull back in this business which will ultimately help, you know, our sales and others who are better prepared to take advantage of an expanded housing market.

But very definitely an improved housing market is the number one answer to improving the - and minimizing the competitive situation that we find today.

Sam McGovern: Got it thanks. That's helpful. And just as a follow-up to some of the M&A questions that were out there, can you talk a little bit about the process, is it an auction typically? Are there a lot of other bidders and specifically I'm curious, one of your sort of national, larger, you know, private competitors has expressed an interest of expanding more into the U.S. south, you know, primarily through M&A. I'm curious as to whether you're seeing any competition from them on the M&A front?

Chad Crow: You know, so far, we've for the most part avoided an auction situation. In one of the deals there was a few other interested parties but even in that deal, we were able to kind of log down a 90 day exclusivity period.

So for the most part we've been able to kind of get in there and do our diligence and avoid the whole auction process.

Sam McGovern: Right, thanks guys. I'll pass it along.

Operator: Our next question comes from Trey Grooms with Stephens Inc.

Trey Grooms: Hey good morning guys and I'm sorry if I missed this too given the phone situation. It was very choppy on the early end of the call. So, you know, given some of the headwinds in SG&A that you've detailed out Chad, you know, kind of looking into next year and I know you said longer-term you continue to see, you know, that kind of a percent of revs that ratio come down but as we kind of look into next year though and your expectation for, you know, about 10% increase in starts I believe, is what Floyd said.

In that environment and, you know, given the current situation with SG&A, would you expect that SG&A leverage to kind of return to, you know, the type of leverage we've been seeing, you know, in periods or is there anything going on now that would kind of mute that somewhat, looking in the next 12 months.

Chad Crow: No, my outlook hasn't changed on our ability to leverage our OPEX even into next year. Like I said, some of it, I think we just prepaid to a degree. Our infrastructure is just out in front of where starts are right now but if we can get the improvement we see or we hope to see in starts next year, then I think it will all fall back into place.

Trey Grooms: And then with your approach that you're, you know, with you guys needing to or taking the approach of walking away from some of this lower margin business, and if you have starts up 10% on average next year, do you think, you know, you've got market share gains in place, you know, from years past and you've done some acquisitions but organically, do you think in that type of environment you should exceed, you know, the end-markets and outperform the end-markets as you have in the past? Or should we expect a more of an in line type of performance?

Chad Crow: I think it's going to be in line to outperform to some degree, somewhere in that range. And I think the acquisitions we've made are certainly going to begin to pay off in that environment and as Floyd said earlier, I think our ability to grow our business, without the constraint of liquidity is going to be to our advantage and an environment where starts are going.

So I think kind of the base case is kind of maintain and I think there's certainly some upside to that.

Floyd Sherman: Yes and I think, you know, still at the end of the day, the one thing that we are going to continue to look to push are margins up. And so that, and you know, it's very difficult to continue to improve your margins when you have as competitive a situation as we do.

And when you're taking market share and still building market, and still building your margin, that's a tough thing to do but it can be done and we've shown that. And I really think that as we go forward, the, we have got to get ourselves positioned so that ultimately on a much smaller housing start basis, and when I talk about that I'm saying a million single family starts, I want to see our margins back up in that traditional area, 24.5 to 25.5%.

And so that would indicate that we have to continue to move it up as the, as the housing market slowly expand and I think we can do that. We've shown this year, we've been able to right now, we're 90 basis points ahead of last year on a housing market that's, you know, relatively flat and I think we can continue the same trend of improving margins and still slightly continuing to improve our market position.

Trey Grooms: And no doubt you guys have done a great job in this environment with your margins. Hats off to you on that and, you know, in that scenario we're talking about 24.5, 25% type gross margins and then also kind of looking at the operating leverage that you have on SG&A.

What does that mean for kind of an EBITDA margin range and at least goals that you guys have in place for that type of environment?

Floyd Sherman: I'll just say the, my - certainly my belief is that we can be north of 8% EBITDA or north of where we were at our height but, you know, if I were to give a range, I'll say north of where we were in 2005, 2006.

Trey Grooms: Okay well thanks for all that color and I appreciate it and good luck guys.

Floyd Sherman: Okay.

Operator: Our next question comes from Jim Fowler with Harvest Capital.

Jim Fowler: Hello gentlemen. Your comments on the compensation to your drivers, can you give a magnitude of change. I think you mentioned that it started to go up in the second quarter and started to ramp in the third-quarter but could you give some context around how much it increased say in the third-quarter from the first-quarter? And then do you think there's more to go as we go to the fourth-quarter and into next year?

And then even further if you might comment on what you think the reality might be if the housing market does pick up? I mean does that put more pressure on compensation for more drivers to come back to the market or, you know, what are your thoughts there? Thanks

Man: Thank you, If housing starts pick up, you know, you will continue to see a tight labor market so there will probably be some ongoing compensation issues but hopefully nothing as significant as we saw from the first-quarter through the third-quarter.

Jim Fowler: Yes, this call's very frustrating with the technology. Hopefully you'll fix that for next quarter. Yes, I'm just interested in the, in, when you comment on the third-quarter versus the second-quarter. Could you put some numeracy around that please?

Male: From the compensation standpoint?

Jim Fowler: For drivers, yes.

Male: Well, as I've said, about a million dollars was incremental. That's on a quarter-over-quarter basis. It wasn't as big of an impact on Q2 to Q3 but we do have over 6 hundred drivers in this company so, you know, it's an important and fairly large part of our head count.

Jim Fowler: And will that, do you expect driver compensation to continue increasing in the fourth-quarter and to start next year or do you think you set it at a level that accommodates the current market?

Male: You know, I'd probably be fooling myself to say there won't be continued pressure on drivers. I think we have a lot of that behind us now but I think there will still be some pressure to some degree.

Jim Fowler: Great, thank you gentlemen.

Operator: It appears we have no further questions in the queue at this time. I would like to turn the conference over to Mr. Sherman for any closing remarks.

Floyd Sherman: Great. We appreciate everyone joining the call today. If you have any follow-up questions, please feel free to give Chad or Marcie a call here in Dallas. Thanks and have a great day.

Operator: That does conclude today's conference. Thank you for your participation.

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