



**Management's Prepared Remarks  
Third Quarter Conference Call  
October 31, 2019**

**Tabitha Zane**

**Vice President, Investor Relations**

On the call today are Jerry Volas, Chief Executive Officer, Robert Buck, President and Chief Operating Officer, and John Peterson, Chief Financial Officer. We have posted senior management's formal remarks on the Investor Relations section of our website at [topbuild.com](http://topbuild.com).

Many of our remarks will include forward-looking statements concerning the company's operations and financial condition. These forward-looking statements include known and unknown risks, including those set forth in this morning's press release as well as in the Company's filings with the SEC. The Company assumes no obligation to update or supplement forward looking statements that become untrue because of subsequent events.

Please note that, other than as otherwise specifically stated, the financial measures to be discussed on this call will be on a non-GAAP basis. The non-GAAP measures are not intended to be considered in isolation or as a substitute for results prepared in accordance with GAAP. We have provided a reconciliation of these financial measures to the most comparable GAAP measures in a table included in today's press release and in the presentation accompanying this call.

**Jerry Volas**

**Chief Executive Officer**

Good morning everyone and thanks for joining us today. We are pleased to report another excellent quarter, as our team continues to do an outstanding job of generating profitable growth.

Before reviewing the quarter, I want to note that, based on recently announced starts, strong household formations and optimistic builder sentiment, the long-awaited acceleration in housing appears to be underway. Low mortgage rates, a pivot by builders to more affordable housing and a strong economy with solid job and wage growth are all factors driving this positive trend. Moreover, the long-term fundamentals, including projected household formations and limited housing supply, point towards continued growth in new home construction.

Our third quarter financial results reflect the strength of our diversified model and our continued focus on improving operational efficiency. Total sales were up 5.4% compared to lagged housing starts that were down 1.0%. Our commercial business again performed extremely well and operating margins at both business segments expanded.

On the capital allocation front, M&A is our number one priority and our focus remains primarily on our core businesses...which are residential and commercial insulation installers and distributors. The synergies we achieve are significant and the opportunity to enhance our market share in regions with strong growth prospects is compelling.



We are also considering expanding our glass product category that encompasses commercial storefronts and residential bath and showers. This business currently contributes approximately \$114 million of annual revenue. Our research and experience validate that this adjacent product category offers many attractive characteristics similar to insulation. While expansion in this area will be independent of our branch insulation network, we will be able to leverage our management expertise, customer relationships and supply chain model.

Looking ahead, our pipeline of acquisition candidates is robust and we expect to bring the best prospects over the finish line in the next couple of quarters.

Our second capital allocation priority is share repurchases. In the third quarter, we repurchased just over 364,000 shares at an average per share price of \$89.76. Since implementing our share repurchase program in 2016, we have repurchased a total of 4.9 million shares at an average per share price of \$56.74.

Consistent with our intent to return capital to our shareholders on a timely basis, we announced a \$50 million accelerated share repurchase which we anticipate executing within the next several days and completing in mid-first quarter. This program reflects management's and our Board's confidence in the long-term potential of TopBuild, our strong future cash flow position and our firm commitment to optimizing the efficiency of our capital structure.

While John will discuss our financial results in further detail, I want to emphasize that our strong operating performance quarter after quarter is the direct result of our uniquely diversified model and the ability of our strong leadership team to manage our businesses well in any general, economic and housing environment.

**John Peterson**  
**Chief Financial Officer**

I'm pleased to report on another excellent quarter of business results delivered by the experienced and talented team to which Jerry just referred.

Starting with consolidated revenue, third quarter results increased 5.4% to \$682.3 million, primarily driven by increased volume and pricing at TruTeam and increased pricing at Service Partners. Revenue for the first nine months of 2019 rose 12.4% to \$1,961.8 million, which includes revenue from acquisitions of \$126.9 million.

Adjusted gross margin increased 130 basis points in the third quarter to 26.3%, and for the first nine months of 2019 expanded 200 basis points to 26.0%.

Adjusted operating profit in the third quarter grew 16.0% to \$80.6 million, with a corresponding margin improvement of 110 basis points. For the first nine months, adjusted operating profit increased 30.6% to \$216.1 million with a corresponding margin improvement of 150 basis points. Both gross margin and operating margin improvements were driven by higher selling prices, strong commercial sales growth, operational efficiencies and synergies from USI, partially offset by higher material costs.



Adjusted EBITDA for the third quarter was \$98.0 million, compared to \$84.3 million in 2018, a 16.3% increase, and our adjusted EBITDA margin improved 140 basis points to 14.4%. In the third quarter, our drop-down to adjusted EBITDA margin for our sales growth was 39.1%.

For the first nine months of 2019, adjusted EBITDA grew 32.7% to \$266.5 million, and adjusted EBITDA margin was 13.6%, a 210-basis point improvement over the first nine months of 2018. Our drop-down to adjusted EBITDA margin during this nine-month period was 30.3% in total and 46.1% on a same branch basis.

Third quarter SG&A as a percent of revenue was 14.5% compared to 14.8% in the third quarter of 2018 and 15.0% last quarter. The year-over-year decrease was primarily the result of lower acquisition and closure costs related to USI.

Adjusted income for the third quarter was \$52.7 million, or \$1.53 per diluted share compared to \$44.0 million in 2018, or \$1.23 per diluted share. Third quarter 2019 adjustments were approximately \$140,000, primarily related to costs associated with the acquisition of Viking Insulation.

Our effective tax rate was 23.2% for the third quarter due to some discrete items captured in the quarter. For long term planning purposes, we still guide to a normalized tax rate of approximately 26.5% which is reflected in our adjusted EPS number of \$1.53 per diluted share as compared to our reported EPS of \$1.60 per diluted share.

For the first nine months of 2019, adjusted income was \$138.8 million, or \$4.02 per diluted share, compared to \$107.1 million in 2018, or \$2.99 per diluted share. Adjustments for the first nine months were \$3.0 million and were primarily associated with the acquisition and integration of USI.

Interest expense in the third quarter 2019 was \$9.5 million and for the first nine months was \$28.7 million.

CAPEX for the first nine months of the year was \$34.1 million, 1.7% of sales, slightly below our targeted long-term range of 2% to 2.5%.

Working capital as a percent of sales for the trailing twelve months was 11.6% versus 11.3% a year ago. This increase was primarily due to the strong growth in heavy commercial which has longer receivable terms and a higher mix of installation business from a year ago which carries higher working capital requirements.

We ended the third quarter with net leverage of 1.64 times trailing 12 months adjusted EBITDA. Total liquidity at September 30, 2019 was \$360.2 million, including cash of \$171.6 million and accessible revolver of \$188.6 million. Operating cash flow was \$182.8 million for the nine months ended September 30.



As Jerry mentioned, our number one choice for our free cash flow is acquisitions and our second is share repurchases. While our pipeline of acquisition candidates is robust, we are also focused on enhancing our capital structure. We have therefore announced a \$50 million Accelerated Share Repurchase (ASR) Program which should be completed sometime in mid-first quarter 2020.

Moving to annual guidance, based on the last two months of starts data and conversations in the field with our customers and branch managers, we've raised our outlook for housing starts for 2019 to a range of 1.245 million to 1.275 million. Our previous outlook was 1.23 million to 1.27 million starts.

In conjunction with this change and as a result of our strong third quarter performance, we've raised both our revenue and adjusted EBITDA outlooks. For revenue, we've raised the low end by \$15 million to \$2,625 million and the high end by \$5 million to \$2,645 million. The low end of adjusted EBITDA has been raised by \$9 million to \$354 million and the high end was increased \$5 million to \$360 million.

**Robert Buck**  
**President and Chief Operating Officer**

Our strong performance, quarter after quarter, is a testament to:

- our team's hard work, alignment and cadence by which we run the business
- our ongoing operational efficiency initiatives,
- our commitment to excellent customer service,
- our strong customer and supplier relationships, and
- our insistence that growth and profit go hand in hand.

Starting with TruTeam's third quarter financial results, sales grew 7.3%, handily beating lagged housing starts which were down 1%. Volume accounted for 3.8% of this growth while selling price increases contributed 3%. TruTeam's adjusted operating margin improved 80 basis points from a year ago to 14.0%.

Service Partners' third quarter sales, were up 3.8%, driven by a 4.4% increase in price, offset by a slight decline in volume. We continue to walk a tightrope between price and volume as we've seen excess fiberglass material flow through to the distribution channels, putting pressure on price. Our team has done a great job managing this balancing act, as evidenced by the 150-basis point increase in Service Partners' adjusted operating margin to 10.6%, the highest adjusted operating margin reported since our spin-off in June 2015.

As we look ahead, the acceleration of starts is positive for both of our business segments and is supported by the continued optimism of our builder customers. As starts continue to climb, which we believe they will, we will continue to leverage our operating platform to help drive solid financial results.



We are also extremely pleased with the strength of our commercial business which once again posted double digit growth. On a same branch basis, commercial revenue grew 18.8% in the third quarter and 21.4% year-to-date. Commercial now accounts for approximately 23% of our total revenue, almost evenly split between heavy and light commercial. As a matter of reference, commercial represented only 16% of our total revenue at the time of the spin.

We plan to continue to grow our commercial business through a number of initiatives. We've mentioned before that light commercial is very similar to residential and most of our branches have the ability to perform this work. Accordingly, we are providing additional resources and tools for our salespeople and branch managers to help them better identify light commercial opportunities and secure additional work.

Acquisitions present another avenue for growth in the commercial space. Over the past few years we've acquired three firms that specialize in heavy commercial insulation, expanding our reach in a number of major cities including Chicago, Los Angeles and San Diego.

We are also planning to green field a handful of new locations specializing in heavy commercial projects. New York is one of our most recent moves. In these greenfield locations we are partnering with a general contractor with whom we have built a previous relationship. As they start up new projects in new geographies, the work is already there for our company to perform and the expense to set up a new location is minimal for us and leads to quicker profitability.

Looking ahead, our commercial backlog remains robust and we are bidding on projects well into 2022.

Before turning the call back to Jerry, I want to touch on a few areas. First is labor, which continues to be tight not only for TopBuild but for all the trades in our industry. We believe we have a leg up on the competition by offering a comprehensive benefits package which helps makes us an "employer of choice." In addition, our ability to share labor among our branches is a major differentiator and gives us a competitive advantage. We are also investing in new areas that we will believe will continue to improve labor productivity.

Second is spray foam which continues to grow but at a slower pace than a year ago as builders pivot to entry level homes in an effort to provide a more affordable product to meet the demands of first-time buyers. As a reminder, although a great solution for our customers, spray foam is about twice the cost of fiberglass insulation.

Finally, our senior leadership team recently undertook an in-depth review of our corporate values and culture. We believe our strong values are a key component of our success and they will continue to guide us as we move forward. They include:

- Putting the safety of our people first
- Delivering results with integrity, respect and accountability
- Focusing on exceeding the expectations of our customers
- Continuously improving and encouraging idea sharing
- Aligning as one team and valuing diversity
- Making a difference in the communities we serve, and
- Empowering our employees to be their best, individually and as a team.



I am extremely proud of our entire TopBuild team for their adherence to these core values and for their focus on working safely to deliver value, quality and service to our customers.

**Jerry Volas**  
**Chief Executive Officer**

Before opening the call up for questions, I wanted to mention that in September, we hosted our annual strategy session with our Board and key members of our leadership and operating teams.

During this two and a half day meeting we take a deep dive into all aspects of our Strategic Plan, with a focus on both short and long-term goals for our Company. Our Board is extremely supportive and the Company's direction and the key tenets of our Plan remain in place:

- Drive top line growth and increase market share in our core residential and commercial installation and distribution businesses,
- Expand existing product adjacencies through a deliberate and measured approach,
- Improve operational efficiency throughout our organization, and
- Make strategic acquisitions that supplement our organic growth.