Management's Prepared Remarks
Second Quarter 2021 Conference Call
August 3, 2021

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Vice President, Investor Relations
On the call today are Robert Buck, President and Chief Executive Officer, and John Peterson, Chief Financial Officer.

We have posted senior management's formal remarks and a PowerPoint presentation that summarizes our comments on the Investor Relations section of our website at topbuild.com.

Many of our remarks will include forward-looking statements which are subject to known and unknown risks and uncertainties, 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, some of 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.

Robert Buck
President and Chief Executive Officer
I want to start by thanking our entire TopBuild team for their continued hard work and dedication. Our strong second quarter performance is a direct result of their commitment to excellence in all that they do.

This continues to be a great operating environment for TopBuild and one that we believe could last for the foreseeable future. Unlike the housing boom of two decades ago which featured excess supply, rampant speculation and weak credit controls, this current housing growth is being driven by strong pent up demand, extremely limited housing inventory, an improving economy and low interest rates.

Governing this growth and elongating the cycle, are material and labor constraints for all trades in our industry. Evidence of this is clearly indicated by completions, which have remained relatively flat over the past year. While we are optimistic some of these supply chain constraints will begin to ease by year-end, the extension of the build cycle has created a healthy backlog.

Turning to our second quarter results, we again demonstrated the strength of our operating model and our ability to pass material cost increases through with selling price adjustments.

Revenue increased 29.1%, 18.3% on a same branch basis, adjusted operating profit grew 55.5% and adjusted EBITDA increased 39.1%. Adjusted operating margin expanded 270 basis points, adjusted EBITDA margin expanded 130 basis points, and adjusted net income per diluted share increased 64.3% to $2.76.

As expected, TruTeam saw a strong sequential increase in customer pricing from the first to the second quarter. With material on allocation and labor constrained, every branch is focused on striking the optimal balance between price and volume, understanding that at the end of the day our goal is driving profitable growth.

Service Partners continues to do an outstanding job managing cost increases and customer pricing, reporting its highest adjusted operating margin since the spin in June 2015. The team also continues to expand its contractor base and grow share with existing customers. John will cover more segment details in his prepared comments.

Turning to material, with fiberglass on allocation, spray foam supplies slowly normalizing and demand remaining strong, we expect both TruTeam and Service Partners to continue to drive higher selling prices throughout the year. Knauf and Johns Manville are on track to bring on their loosefill lines in the fourth quarter and current capacity is under constant review within the industry.

Our commercial business in both segments continues to improve as delayed projects resume and new projects are initiated. Bidding activity for both light and heavy commercial remains strong and our backlog is healthy. On a same branch basis, commercial revenue increased 20.8% compared to the second quarter of last year, marking the fourth consecutive quarter of commercial revenue improvement. Our heavy commercial teams are busy and the types of projects we are winning and working on include health care facilities, large distribution centers and warehouses.

Regarding light commercial, as residential homes are built, demand for services such as restaurants, strip malls, and other infrastructure to support these new communities should grow significantly. The vast majority of our residential branches perform light commercial installation and the teams at our local branches are keenly aware of these opportunities and the importance of establishing relationships with the small general contractors in their respective markets who control these types of projects.

We remain very bullish with regards to the $5 billion commercial market, both heavy and light, and we expect our commercial business will continue to strengthen as we move through the year.

On the capital allocation front, we completed three acquisitions in the second quarter, American Building Systems, Creative Conservation, both of which we discussed on our last call, and RJ Insulation which closed in June and is expected to generate approximately $4 million in annual revenue. Year-to-date, we've completed five acquisitions which are expected to generate approximately $221 million of revenue on a pro-forma full year basis.

Over the past six years we have acquired 19 companies that combined are generating over $800 million of annual revenue and they are creating tremendous value for our stakeholders. During this same period, we expanded and enhanced our M&A team, and the integration of acquisitions is a core competency. Our focus remains on acquiring well-run installation and distribution companies around our core of insulation as well as related adjacent products. With a robust pipeline of prospects, we expect to stay very busy on this front through 2021.

We also used our capital in the second quarter to repurchase almost 74,000 shares and year-to-date we've repurchased 123,000 shares. We are pleased that our Board of Directors approved a new, $200 million share repurchase program, demonstrating a high level of confidence in our financial performance and our strong cash generation. Since implementing our first share repurchase program in 2016, we have returned over $410 million to our shareholders.

One area that is growing increasingly important for all stakeholders is ESG. This remains a priority and we recently dedicated additional resources towards these efforts. Our approach includes:

- Maintaining our focus on safety and continuing to improve the well-being of our employees,
- Ensuring that our workforce reflects the diversity of the communities in which we operate,
- Incorporating energy efficient solutions in our residential and commercial projects, and
- Tracking and reporting energy usage and waste generation across our footprint.

On the environmental front, in addition to our core insulation business which drives improved energy efficiency in all of the communities in which we operate, I would remind you of our TopBuild Home Services group which is at the forefront of building science and building code compliance. Our expertise in this area is concentrated on advancing environmentally conscious construction. For example, our Environments For Living® program helps builders construct high-performance houses that save energy and reduce greenhouse gas emissions. In addition, our extensively trained Home Energy Raters provide the evaluation, testing and independent verification required to be considered an ENERGY STAR compliant home.

Before turning the call over to John, I wanted to note that in late June we were pleased to learn that TopBuild was moving from the Russell 2000 to the Russell 1000 index. Some of you may remember that at the time of the spin in June 2015, our market cap was approximately $1.1B. Today it is over $6 billion, more than a 450% increase. This move is clearly a recognition of our strong growth and the tremendous value we have created for our stakeholders over the past six years. Looking ahead, we are confident in our ability to grow our business and continue to provide great value for our stakeholders.

John Peterson
Chief Financial Officer
As Robert noted, this is a great operating environment for TopBuild and our strong second quarter results provide solid evidence of the strength of our business model and our ability to successfully manage and optimize our input costs and pricing as well as our overall cost structure.

Moving to our results, in the second quarter, net sales increased 29.1% to $834.3 million primarily due to an 11.8% increase in sales volume, a 6.5% increase in price and $70.2 million of revenue from six acquisitions; Garland, LCR, Ozark, ABS, Creative Conservation and RJ Insulation. For the first six months of 2021, net sales increased 21.4%, primarily driven by increased selling prices, sales volume and $97.6 million of revenue from acquisitions.

Adjusted gross margin increased 140 basis points in the second quarter and 90 basis points in the first half of 2021 to 29.2% and 28.0%, respectively, driven by higher selling prices, lower depreciation expense and insurance costs, partially offset by material inflation. On a same branch basis, adjusted gross margin expanded 190 basis points in the second quarter.

Adjusted operating profit in the second quarter grew 55.5% to $129.9 million, with a corresponding margin improvement of 270 basis points to 15.6%. For the first six months, adjusted operating profit increased 47.7% to $227.1 million with a corresponding margin improvement of 260 basis points.

Adjusted EBITDA for the second quarter was $149.8 million, compared to $107.8 million in the second quarter of 2020, a 39.1% increase, and adjusted EBITDA margin expanded 130-basis points to 18.0%. As a reminder, in the second quarter of last year our depreciation expense was approximately $5 million higher due to a reduction in the carrying value of older assets that the Company was no longer utilizing.

For the first six months of 2021, adjusted EBITDA grew 35.5% to $265.7 million, and adjusted EBITDA margin was 16.8%, a 170-basis point improvement over first half 2020.

Second quarter SG&A as a percent of sales was 13.8% compared to 15.1% in the second quarter of 2020. The year-over-year decrease was primarily the result of higher sales, lower share-based compensation, and lower legal fees.

Adjusted income for the second quarter was $91.6 million, or $2.76 per diluted share, compared to $55.7 million, or $1.68 per diluted share. For the first six months of 2021, adjusted income was $158.7 million, or $4.78 per diluted share, compared to $101.6 million, or $3.04 per diluted share.

Second quarter adjustments to net income were $1.6 million, primarily related to acquisition expenses. Adjustments to net income in the first six-months of 2021 were $16.7 million, primarily tied to $13.9 million of debt refinancing costs and the remainder related to acquisition expenses and the COVID-19 Leave Plan initiated last March.

Our effective tax rate for the quarter was 26.1% and 24.0% for the first six months of the year.

Interest expense in the second quarter of 2021 was $6.1 million compared to $8.3 million in the prior year, primarily driven by lower interest rates on our New Senior Notes and borrowings under the Amended Credit Agreement.
CAPEX for the second quarter was $16.3 million, or 2% of sales, and for the first six months was $28.6 million or 1.8% of sales, consistent with our long-term guidance of 2% of sales.

Working capital as a percent of trailing twelve-month sales was 9.9% versus 10.5% a year ago. This decrease was due to improvement in past due accounts receivables at both TruTeam and Service Partners.

We ended the second quarter with net leverage of 0.9 times, using trailing 12 months adjusted EBITDA. Total liquidity at June 30, 2021 was $640.5 million, including cash of $261.7 million and accessible revolver of $378.8 million. Operating cash flow was $202.2 million for the six months ended June 30.

Now let's turn to our segment results.

TruTeam's sales increased a robust 29.8% in the second quarter to $605.6 million. On a same branch basis, revenue grew 15.4%. The increase in sales was driven by revenue from acquisitions, same branch volume growth, and higher selling prices. Second quarter adjusted operating margin for TruTeam was 16.6%, a 140-basis point improvement.

Service Partners' second quarter sales were up a strong 26.4% to $273.4 million, driven by an increase in both volume and higher selling prices, and to a lesser degree, acquisitions. Second quarter adjusted operating margin for Service Partners was 15.7%, a 410-basis point improvement from 2020.

Moving to 2021 annual guidance; based on builder orders, commercial activity, low housing inventory, and anticipated low interest rates, we remain optimistic this will be a very good year for residential and commercial construction and TopBuild will benefit from this healthy environment. However, as we noted in May, our guidance assumes some level of industry wide material and labor constraints, which have already led to an extended build cycle and higher than normal backlog. On the flip side, these constraints, coupled with low inventory and strong demand, should lead to a healthy residential and commercial construction environment for the foreseeable future.

Based on our first half results, acquisitions completed since our last earnings release, and internal forecasts, we are now projecting total sales to be between $3,290 million and $3,370 million, a $70 million increase on the low end of the range and a $50 million increase on the high end. Adjusted EBITDA is now expected to be between $565 million and $590 million, a $33 million increase on the low end of the range and a $28 million increase on the high end. This assumes a range of residential new housing starts of between 1.475 million and 1.525 million, which is an increase from first quarter guidance based on recent housing activity.

Robert Buck
President and Chief Executive Officer
Thank you, John. Our entire company remains focused on achieving profitable growth through operational excellence and thoughtful and balanced capital allocation. As we look to the rest of the year, we expect solid full-year performance at both TruTeam and Service Partners. The housing market is strong, fueled by low interest rates, pent up demand and very little inventory. This is a good operating environment for TopBuild and should remain so for the foreseeable future.

As always, I thank the entire TopBuild team for their focus on working safely to deliver value, quality, and service to our customers.