



Twin Disc, Inc.

Twin Disc Announces Strategic Acquisition

June 13, 2018

C O R P O R A T E P A R T I C I P A N T S

Stan Berger, *Moderator, SM Berger & Company, Inc.*

John Batten, *President & Chief Executive Officer*

Jeffrey Knutson, *Vice President of Finance, Chief Financial Officer, Treasurer & Secretary*

C O N F E R E N C E C A L L P A R T I C I P A N T S

Timothy Wojs, *Robert W. Baird & Company, Inc.*

Mario Gabelli, *Gabelli & Company*

P R E S E N T A T I O N

Operator:

Good day, everyone, and welcome to the Twin Disc Announces Strategic Acquisition Call. Today's conference is being recorded. At this time I would like to turn the conference over to Mr. Stan Berger. Please go ahead, sir.

Stan Berger:

Thank you, Jenny (phon). On behalf of the Management of Twin Disc, we're extremely pleased that you've taken the time to participate on our call. Thank you for joining us to discuss the Company's acquisition of Veth Propulsion Holding, BV.

Before I introduce Management, I would like to remind everyone that certain statements made during the course of this conference call, especially those that state Management's intentions, hopes, beliefs, expectations or predictions for the future, are forward-looking statements. It is important to remember that the Company's actual results could differ materially from those projected in such forward-looking statements. Additional information concerning factors that could cause actual results to differ materially from those in the forward-looking statements are contained in the Company's Annual Report on Form 10-K, copies of which may be obtained by contacting either the Company or the SEC.

By now you should've received a copy of the news release announcing the acquisition of Veth Propulsion which was issued this morning before the market opened. If you have not received a copy, please call Annette Mianeck. The phone number is 262-638-4000, and she will send a copy to you.

Hosting the call today are John Batten, Twin Disc President and Chief Executive Officer, and Jeff Knutson, the Company's Vice President of Finance, Chief Financial Officer, Treasurer and secretary.

At this time I will turn the call over to John Batten. John?

John Batten:

Thanks, Dan. Thank you everybody for coming on this call on relatively short notice on the press release this morning. Today's announcement of our intent to acquire Veth Propulsion is an extremely exciting day for us. This was the culmination of really up to a five-year process of identifying where our marine markets were going, the technology and the products that we were going to need in the future. In many cases, the future is right now as hybrid technology, diesel electric technology is working its way down the horsepower spectrum and into vessels that have typically been standard marine propulsion.

We looked at many companies who had this technology and we felt early in the process that Veth was going to be the best fit for us. We started a relationship with them two years ago and distributing their products in North America and in Asia, so we've come to understand each other and get to know each other better over those two years. The majority of Veth's existing businesses are in the European markets and they have not expanded as much in North and South America and in Asia. Combining Veth's product with our international global distribution network, which is extensive in North America, South America and Asia, we feel we have a very excellent chance of growing their business and growing our business in these marine markets significantly. A lot of the overlap and technology that we're looking at, clearly they have the diesel electric technology, they have hybrid experience, and we're seeing more and more of that in our space. Just, in general, they have 60 years of experience in the marine in primarily the European markets.

This, as you've gone through the press release, you'll see that greatly expands our marine product line and we could not be happier. Obviously we did not address the industrials or the transmission market and we continue to look for opportunities there, but we have a lot of work to do combining and creating the synergies that we have identified in this deal.

With that, those are the opening comments and Jeff and I are here and top and direct (phon), after meeting with the employees of Veth, and we're ready to take your questions now. Jenny, you can open up the line.

Operator:

Thank you. If you'd like to ask a question, please signal by pressing star, one on your telephone keypad. If you're using a speakerphone, please make sure that your mute function is turned off to allow your signal to reach our equipment. Again, press star, one to ask a question. We'll pause a moment so that everyone has an opportunity to signal for questions.

We'll hear first from Tim Wojs of Baird.

Timothy Wojs:

Hey, guys. Good morning or good afternoon.

John Batten:

Good morning, Tim.

Jeffrey Knutson:

Good morning, Jim.

Timothy Wojs:

Hey, congrats on the acquisition. Maybe just my first question: could you just talk a little bit more about the historical kind of relationship between you and Veth? Does any of that kind of change going forward or is it just now that you kind own the business?

John Batten:

Well, really, we had identified them as a potential partner almost five years ago, but you can't force something before it's time. The timing has to be right and certainly the downturn that we saw two years ago in our Oil and Gas business and Asian business didn't really make it the right time. But certainly it was the right time for us to get to know each other better through the distribution agreement. It gave us a chance to better understand their product, the process of selling the product, and, really, what the service requirements were going to be around the world. Those last two years certainly weren't wasted at all, very beneficial and we feel that the two years that we've spent as a distributor for them certainly helped us as we start a new relationship on July 2.

Timothy Wojs:

Right. No. Okay. I think it's about \$60 million of revenue. Is that a net revenue number because you do do some—is that a net number that you guys would recognize through your P&L

Jeffrey Knutson:

Yes. Yes. That's that number, Tim.

Timothy Wojs:

Okay. Is there any sense you can give us for what maybe the growth rate has been in this business over the last couple of years and how the margins have performed?

Jeffrey Knutson:

Well, I think they went through a bit of a dip when we had our downturn back in 2015, but they recovered very quickly. I think they had 10% growth from '15 to '16 and projecting very strong growth in 2017. Margin performance has been very consistent. Their margin performance only dipped slightly through the downturn and what we've seen is they've been able to take market share during their recovery in still difficult markets by—and maintaining their margins in a real nice range. We're expecting margins right around our typical margins, so the low- to mid-30s, and that's where they've been consistently over the past several years.

Timothy Wojs:

Okay. Then on the synergies, are those all cost synergies?

John Batten:

No.

Jeffrey Knutson:

No. The synergies are really more focused on market and growth and opportunities we see for both our products to be sold along with the Veth products and vice versa.

Timothy Wojs:

Okay.

John Batten:

Really, some engineering expense that we will probably be able to avoid in the future by leveraging their platform across the broader product line.

Timothy Wojs:

Got you. Okay. That's more of like an EBIT number for some of the sales synergies, potentially is kind of what you're projecting there?

Jeffrey Knutson:

Yes.

Timothy Wojs:

Okay. Then the last, just, question for me is just the interest rate you're assuming on debt and then just tax rate, how should we think about that?

Jeffrey Knutson:

The tax rate we're assuming is 25%. The interest rate that we're projecting, and we're still working through as I think you would've noticed in the press release, we're still finalizing the financing, but we're projecting that to be somewhere in the 4.5%, 4.7% blended rate range.

Timothy Wojs:

Okay. Great. Well, congrats on the deal and good luck on integration.

John Batten:

Thank you.

Jeffrey Knutson:

Thanks, Tim.

John Batten:

Thanks, Tim.

Operator:

Our next question comes from Mario Gabelli of Gabelli and Company.

Mario Gabelli:

Hey, John. Just a couple of quick questions. Unfortunately I got on a little late. You're talking about \$60 million acquisition. Have you hedged the currency in anticipation of the deal or you're just working on that in the closing?

John Batten:

We're working on that towards closing, Mario.

Mario Gabelli:

Any unusual accounting issues? Before I get into—I'd like to go into the weeds first and then go upstairs.

Jeffrey Knutson:

No. Really (inaudible) no.

Mario Gabelli:

Okay. Are you buying assets or are you buying a C Corp equivalent?

Jeffrey Knutson:

We're buying stock, so (inaudible).

Mario Gabelli:

Is it a partnership, an LLC, a C Corp?

Jeffrey Knutson:

It's a BV, so in and (inaudible).

Mario Gabelli:

Yes. All right. I got it. (inaudible). The equivalency is from a tax point of view, no step (inaudible).

Jeffrey Knutson:

Right. Yes.

Mario Gabelli:

Just so I get a quick 101, what do they serve, what's the addressable market, and how do I get a handle on those details so my analysts can drill down a little better?

John Batten:

I would say that their addressable market certainly is in, depending upon how big we go in these estimate (phon) thrusters, certainly is in the \$750 million range.

Mario Gabelli:

Yes, but give me an example of who they sell into, okay; give me a 101.

John Batten:

Sure. Where we sell our standard gearboxes into a fast supply vessel for C Corp (phon), offshore oil rigs—I'm using an oil and gas example—(inaudible).

Mario Gabelli:

Go ahead.

John Batten:

Yes. Azimuth (phon) thrusters would be used on the OFDs, the displacement vessels, the big anchor-handling tugs. You'd also see the azimuth thrusters on the inland waterways of Europe, the shipping, the container ships going up and down the Rhine.

Mario Gabelli:

Okay. These are not on the naval (inaudible) type that you don't find those on those kind of applications that they're building up a large fleet there around the world, military (inaudible)?

John Batten:

Correct, no. Our applications would be smaller than that.

Mario Gabelli:

Yes. Okay. So this is basically commercial and so on?

John Batten:

Yes.

Mario Gabelli:

So that would cover that question. I will catch up and read the conference call notes on something that I might've missed and look forward to comparing notes. You haven't talked about the overall impact of what's going on in the Bakken (phon) but the oil patch in terms of your traditional business, or that's for another meeting?

John Batten:

That's for another meeting and (inaudible).

Mario Gabelli:

Thanks, John. Thanks and go back and fine tune everything you're doing. Terrific. Thank you.

John Batten:

All right. Thank you, Mario.

Operator:

As a reminder, you may press star, one on your telephone keypad if you do have a question at this time; that is star, one. We will pause a moment.

At this time there are no further questions in the queue. I will turn the call back over to John Batten at this time for any additional or closing remarks.

John Batten:

All right. Well, thank you, everyone. Again, we appreciate you tuning in on short notice. We will obviously have a lot more information and presentation and discussion and open for questions at the close of our

fourth quarter—actually, no, third quarter—fourth quarter. Thanks for tuning in everyone and thanks for your continued interest. Jenny, we're all done.

Operator:

Again, that does conclude the call. Thank you for your participation. You may now disconnect.