CORPORATE PARTICIPANTS

Greg Yull
Chief Executive Officer

Jeff Crystal
Chief Financial Officer

CONFERENCE CALL PARTICIPANTS

Michael Doumet
Scotiabank

Ben Holton
RBC Capital Markets

Ben Jekic
GMP Securities

PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. Welcome to Intertape Polymer Group's Second Quarter 2016 Results Shareholder's Conference call.

During the call, all participants will be in a listen-only mode. Afterwards, we will conduct a question and answer session. In order to maximize the efficiency of this event, the question period will be open to financial professionals only. At that time, those with questions should press star followed by the number one on their telephone keypad. If at any time during the conference you need to reach an operator, please press star followed by zero.

Your speakers for today are Greg Yull, CEO, and Jeff Crystal, CFO.

I would like to caution all participants that in response to your questions and in our prepared remarks today we will be making forward-looking statements which reflect management's beliefs and assumptions regarding future events based on information available today. The company undertakes no duty to update this information, including its earnings outlook, even though its situation may change in the future. You are therefore cautioned to not place undue reliance on these forward-looking statements as they are not a guarantee of future performance and are subject to a number of risks and uncertainties that could cause actual results to differ materially from those expected. I encourage you to review the discussion of the risks factors and uncertainties contained in the company's security filings in Canada and with the Securities and Exchange Commission.

During this call we will also be referring to certain non-GAAP financial measures as defined under the SEC rules, including adjusted EBITDA, adjusted net earnings, and adjusted net earnings per share. A reconciliation of the non-GAAP financial measures to the most directly comparable GAAP measures is available at our website at www.intertapepolymer.com and are included in its filings, including the MD&A filed today.

I would like to remind everyone that this conference is being recorded today, Thursday, August 11, 2016, at 10:00 a.m. Eastern Time and will now turn the call over to Greg Yull. Mr. Yull, please go ahead, sir.

Greg Yull, Chief Executive Officer

Thank you, operator, and good morning, everyone. Welcome to Intertape's 2016 second quarter results conference call. Joining me is Jeff Crystal, our CFO. After our comments, Jeff and I will be happy to answer any questions you may have.

During the call we will make reference to our quarterly earnings presentation that you can download from the Investor Relations section of our website.

I will begin with a brief review of the highlights for the quarter starting on pages three and four of our presentation.

We are very pleased by our results for the quarter. Our operations performed above our expectations. We were seeing manufacturing cost reduction initiatives positively impacting the overall performance of our various manufacturing facilities, as well as the benefits from the spread between selling prices and raw material costs. We are also seeing growth from e-commerce fulfillment across our packaging product offerings. Furthermore, the Better Packages and TaraTape acquisitions completed last year are performing very well and in both cases are exceeding our expectations in terms of EBITDA contributions; however, we continue to have ongoing challenges in our woven business, our international customer channel, and most recently in the masking tape production ramp up in the Blythewood facility. All of this considered, we reported one of the highest levels of adjusted EBITDA in our history of $33 million. This equates to approximately $30 million when excluding the impact of the South Carolina flood and related insurance proceeds.

When compared to Q2 2015, revenue increased by 2.5 percent to $201.5 million. The increase was due to additional revenue derived from the TaraTape acquisition, the decrease in South Carolina commissioning revenue reduction, and increased sales volume, partially offset by a decrease in average selling price. Here again we achieved revenue growth despite an estimated $5 million impact of lost sales of masking tape and stencil products from the South Carolina flood. Gross margin increased to 25.7 percent from 21.6 percent compared to Q2 2015. Without the estimated positive impact of the South Carolina flood and related insurance proceeds of $3 million, the gross margin was still a very healthy 23.8 percent. The increase was driven in large part by manufacturing cost reduction initiatives and the increase in the spread between selling prices and raw material costs. Adjusted net earnings increased $6.2 million to $20.3 million in Q2 2016, primarily due to an increase in gross profit and the contribution from acquisitions partially offset by higher SG&A. We estimate that adjusted net earnings were positively impacted by the South Carolina flood and related insurance proceeds by approximately $2 million. Adjusted EBITDA increased by 21.7 percent to $33 million and was in line with our guidance. These solid results were achieved despite a very modest positive contribution from the cost savings at the Blythewood facility.

Now on page seven, in July we renewed our NCIB for 12-month period starting July 14, 2016, under which we can repurchase up to 4 million common shares for cancellation. Since July 2014 we have repurchased 3.2 million shares representing a total amount of 39.5 million. During the second quarter and as of August 10, 2016 no shares were repurchased under the NCIB and we still intend to be opportunistic in executing any share repurchases over the next 12 months. Finally, the Board of Directors amended the company's dividend policy to increase the annualized dividend by 7.7 percent from $0.52 to $0.56 per common share. The Board's decision to increase the dividend was based on the company continued strong financial position and positive outlook. Since the dividend policy was reinstated in August 2012 the company has increased the annual dividend four times and paid out a total of $88.3 million in dividends to our shareholders.

Turning to page eight, capital expenditures year to date in 2016 were $23.3 million. During the year water-activated tape, shrink film, and specialty tape projects accounted for 30 percent of that total amount. To date, these projects are all progressing according to announced timelines and budgets. For 2016, in line with our previous guidance, we expect CapEx to be in the range of $55 million to $65 million, of which $8 million to $12 million is expected to be used to support maintenance needs.

On page nine, our manufacturing cost reductions totalled $6.2 million year to date and we expect total cost reductions for 2016 of between $8 million and $11 million, excluding any cost savings related to the South Carolina project.

At this point I'll turn the call over to Jeff, who will provide you with additional insights into our financials. Jeff?

Jeff Crystal, Chief Financial Officer

Thank you, Greg.

I would now like to refer you to page 10 of the presentation, where we present a summary of our results for the second quarter of 2016.

Gross profit totalled $51.8 million in the second quarter of 2016, an increase of 22.2 percent from $42.4 million a year ago. Gross margin was 25.7 percent in the second quarter of 2016 and 21.6 percent in the second quarter of 2015. Gross margin increased in the second quarter of 2016 primarily due to South Carolina flood insurance claim settlement proceeds, the favourable impact of the company's manufacturing cost reduction programs, and an increase in the spread between selling prices and lower raw material costs.

The South Carolina flood insurance claim proceeds received in the second quarter were $5 million, of which $4.5 million was recorded as a reduction in cost of sales and $0.5 million as a reduction of manufacturing closures, restructuring, and other related charges. On a sequential basis, gross margin increased to 25.7 percent from 21.5 percent in the first quarter of 2016 primarily due to South Carolina flood insurance claim settlement proceeds and unfavourable product mix variance.

SG&A was $26.3 million for the second quarter of 2016, an increase of 18.1 percent from $22.3 million a year ago primarily due to an increase in variable compensation expense employee-related costs to support business growth initiatives, and additional SG&A derived from the TaraTape acquisition. On a sequential basis, when compared with the first quarter, SG&A increased 12.4 percent primarily due to an increase in variable and stock-based compensation expense. Adjusted net earnings increased to $20.3 million for the second quarter of 2016 from $14.1 million in the second quarter of 2015.

The $6.2 million increase was primarily due to an increase in gross profit and the acquisitions of Better Packages and TaraTape partially offset by increases in SG&A.

For the second quarter of 2016 the effective tax rate was 29.1 percent versus 28.8 percent in the second quarter of 2015. The increase in the effective tax rate compared to 24 percent in the first quarter of 2016 was mainly due to variations in the geographic mix of earnings between the two periods. Assuming there are no material changes to the company's expected geographic mix of earnings over the remainder of the fiscal year, the company still expects its effective tax rate for the full financial year of 2016 to be between 25 and 30 percent.

As indicated on page 13 of the presentation, adjusted EBITDA totalled $33 million for the second quarter of 2016 a 21.7 percent increase from $27.1 million in the second quarter of 2015 primarily due to an increase in gross profit partially offset by the increase in SG&A. On page 15, adjusted EBITDA increased sequentially by 37.3 percent from $24 million in the first quarter of 2016, primarily due to those same drivers.

As you will note on page 18, cash flows from operations decreased in the second quarter of 2016 by $1.4 million to $24.4 million from $25.7 million in the second quarter of 2015, primarily due to an increase in trade receivables and a decrease in accounts payable partially offset by an increase in gross profit. Sequentially, we experienced the large increase in cash flows from operations and free cash flows, mainly due to a large seasonal increase in working capital in the first quarter of 2016 and an increase in gross profit in the second quarter of 2016.

Free cash flows decreased in the second quarter of 2016 by $9 million to $10.6 million from $19.6 million in the second quarter of 2015 primarily due to an increase in capital expenditures. Net debt at June 30, 2016 was $154.4 million, an increase of $19.2 million compared to December 31, 2015 primarily to fund our working capital requirements, CapEx, and dividend payments, partially offset by cash flows from operating activities before changes in working capital. As of June 30, 2016 the company had cash and loan availability under its revolving credit facility of $162 million. This compares with cash and loan availability of $182.3 million as of December 31, 2015.

Days inventory increased by 5.9 percent to 68 in the second quarter of 2016, compared to 64 in the second quarter of 2015. Inventories increased $10.6 million to $111.2 million as of June 30, 2016 from $100.6 million as of December 31, 2015. The increase was primarily due to an inventory build in anticipation of higher expected sales volume and annual maintenance shutdowns of certain facilities in the third quarter of 2016 as well as an increase in raw material purchases. Days sales outstanding increased to 40 in the second quarter of 2016 compared to 39 in the second quarter of 2015. Trade receivables increased $9.5 million to $88 million as of June 30, 2016 from $78.5 million as of December 31, 2015, primarily due to an increase in the amount of revenue invoiced in the second quarter of 2016 as compared to the fourth quarter of 2015.

Greg will now provide further details on the Columbia facility, the South Carolina project, and our outlook. Greg?

Greg Yull, Chief Executive Officer

Thanks, Jeff.

On page 19 we provide an update on the Columbia, South Carolina flood. The company, along with its insurers and advisors, continue to assess the damage. We've received a total of $10 million in insurance claim settlement proceeds to date since the fourth quarter of 2015. We continue to believe that our insurance policies will substantially cover our flood-related losses and we have been filing claims as we work through the cost and supporting documents related to the damage suffered by the company. We're aiming to resolve most of the insurance claim settlement process in 2016 but are unable to predict the amount and timing of the total recovery.

On page 20 is our update on the South Carolina project. The duct tape production is meeting targeted production levels and has contributed a net positive impact on gross profit and adjusted EBITDA in the quarter for the first six months of 2016. In regards to masking tape production, we've been working on optimizing the related production processes since production was transferred in the fourth quarter of 2015. Since that time we've made significant improvements towards that objective; however, since the end of the second quarter of 2016 the company has made significantly less progress than expected on reducing the inefficiencies in masking tape production as well as eliminating certain quality issues related to one of the masking tape products. These masking tape production inefficiencies largely offset the cost saving realized by the duct tape production, resulting in only a slightly positive impact to the results realized in the second quarter of 2016. This was a setback when compared with the first quarter of 2016; therefore, at this stage, we believe the ramp-up period of masking tape could be extended and possibly generate less cost savings than initially anticipated. We are working aggressively on several initiatives that should yield positive results and will provide further updates towards the end of the year. For fiscal 2016 we still expect the cost savings from the South Carolina project to have a significant net positive impact on gross profit and adjusted EBITDA compared to 2015 given the success of the duct tape production and the expected improvements to masking tape production. As I have stated, we'll provide updates as we better understand what this means regarding the full realization of the approximately $13 million of cost savings expected to be realized by the beginning of 2017.

Moving on to page 21, we have our outlook for the remainder of 2016. Our annual guidance for 2016 is mostly unchanged since our last announcement. We expect gross margin for 2016 to be between 23 percent and 24 percent. Considering year-to-date results and expectations for the second half of the year we have raised the bottom end of our gross margin range to 23 percent from 22 percent. Adjusted EBITDA is still expected to be between $117 million to $123 million, excluding the impact of the South Carolina flood. In terms of our Q3 2016 results, excluding the impact of the South Carolina flood we expect revenue, gross margin, and adjusted EBITDA in the third quarter of 2016 to be greater than in the third quarter of 2015.

In conclusion, we remain optimistic for the remainder of fiscal 2016 and our focus on achieving our long-term goal to significantly grow the company over the next five to seven years. This completes my presentation. At this point Jeff and I will open up the call to questions. Operator?

QUESTION AND ANSWER SESSION

Operator

Thank you. Ladies and gentlemen, we will now conduct the question and answer period for analysts. If analysts would like to register a question, please press star followed by the number one on your telephone keypad. You will hear a one-tone prompt to acknowledge your request. If your question has been answered and you would like to withdraw your registration, please press pound on your telephone keypad. If you are using a speakerphone, please lift your handset before entering your request. One moment please for the first question.

Your first question comes from the line of Michael Doumet from Scotiabank. Your line is open.

Michael Doumet, Scotiabank

Hi. Good morning, guys. Well done in the quarter.

Greg Yull, Chief Executive Officer

Good morning. Thanks.

Michael Doumet, Scotiabank

So I'm going to jump to Blythewood here. You've indicated that you've made, if I understood this correctly, significant improvements on the masking tape production throughout the quarter in Q2.

Jeff Crystal, Chief Financial Officer

No.

Michael Doumet, Scotiabank

No. Okay. So to that $0.2 million positive, is that equivalent to your exit run rate as well as in terms of profitability?

Jeff Crystal, Chief Financial Officer

No. So that just represents what we had in the quarter, so that represents the positive impact of duct less the negative impact of masking in the quarter. What we said is that basically since the beginning when moved masking tape there in Q4 of 2015, since then we had made significant improvements, but we haven't made those improvements at the same rate certainly over the last couple of months and that's where these inefficiencies are coming from.

Michael Doumet, Scotiabank

So currently exiting the quarter you're near that breakeven point if I understood that correctly.

Jeff Crystal, Chief Financial Officer

Yes, exiting the quarter yes.

Michael Doumet, Scotiabank

Okay. Could you maybe break that down to, so duct tape seems to be achieving the cost savings, could you give us a sense if masking tape is at least headed to a neutral or breakeven in the coming quarters, just to give us a sense of how that ramps up throughout the year?

Greg Yull, Chief Executive Officer

Well, what I would say is that we feel confident in the plan in place. We believe that we're going to see improvement as we move through the year. It's hard to determine, because we are, like I'm sure everyone is, frustrated with a lack of progress in the last month or two, but we believe that there is a plan in place. We believe there are good people in place executing that plan. And at this point we're not going to give guidance as it relates to how that ramps up through the year. But, again, I'm confident that at the end of the project, which should be soon, we'll get to a very profitable plan. So very confident in the technology, still confident in the people.

Michael Doumet, Scotiabank

Okay. Fair enough. So maybe switching over to the lost sales relating to the South Carolina flood, that was a $5 million, similar to last quarter. How do you feel in terms of getting that number back to zero before October?

Greg Yull, Chief Executive Officer

Well I think you've got a couple other things playing in there. You've got a currency issue coming out of the U.S. plant. I think we should make some headway. We've got good progress on time in our stencil production right now, so we should be back in production of that product line within the next week or two. So we feel confident about that. And I think we should see some ramp up of that lost sales or minimization of the lost sales as we move into October/November.

Michael Doumet, Scotiabank

Okay. And maybe another question related to that, just based on the precedence established in regards to the insurance claims this quarter, do you expect the flood impact to be largely neutral on gross margins, maybe even into 2017 but throughout the time period?

Greg Yull, Chief Executive Officer

We hope so.

Michael Doumet, Scotiabank

Okay. And maybe I just have one last one last question before I pass it on here. Now we've seen lower resin prices for the last approximately 18 months. That could go lower but just excluding that how should we look at margins going forward and maybe the incrementals or maybe no more incrementals in terms of an increased spread and price and costs?

Greg Yull, Chief Executive Officer

Yes, tough to give guidance on that. I think you got to look at our gross margin guidance there. But from a raw material perspective, when we think of what we're going to incur in Q3 compared to Q2, there are some increases going through on polyethylene potentially. Polypropylene is probably moving a little lower. We're seeing a little movement up in some hydrocarbons but net-net there is not a big impact on raw material sequentially in our business.

Michael Doumet, Scotiabank

Okay, perfect. That's it for me. Thanks, guys.

Operator

Our next question comes from the line of Ben Holton from RBC Capital Markets. Please proceed with your question.

Ben Holton, RBC Capital Markets

Thanks and good morning, guys. It looks like you have very solid operations outside of South Carolina and, not to detract from that but I also have a few South Carolina questions. So I apologize in advance for those. Looking to Blythewood, what has changed since the Investor Day in late June that's driving the more negative outlook on the masking tape ramp and cost savings? Is that simply projected progress that didn't happen or was there a step back somewhere?

Greg Yull, Chief Executive Officer

I think it's a combination of two. It's the lack of progress from that day and then we also ran into, just after that timeframe we ran into some quality issues with one of our products, and that had an impact as well.

On a go-forward basis we feel like we have a good recovery plan on the product as it relates to the quality issues, but we're really just not seeing the reliability and repeatability of the process as it relates to run time. And we've covered this before but if you don't get your runtime and you don't have your machine running at an optimal level, you create downstream waste and other cost associated with the line, and so I would say that it's a lack of progress from that June period to today.

Ben Holton, RBC Capital Markets

All right. And can you remind us what proportion of, I guess, the plant's revenue is tied to masking tape? And then, similarly, what proportion of that planned $13 million savings, what's expected to come from the masking tape line?

Greg Yull, Chief Executive Officer

Yeah, so the revenue we didn't disclose but the cost savings, as you know, split pretty much 50/50 between duct tape and masking tape.

Ben Holton, RBC Capital Markets

And just to be clear, I guess, do you expect the masking tape line to still present some sort of cost savings just lower than initially thought or is there a risk, an outside risk, that it could end up being earnings drag versus the process at Columbia?

Greg Yull, Chief Executive Officer

Well, I think it's positive. Absolutely.

Ben Holton, RBC Capital Markets

Okay. Thanks. I'll pass the line here.

Operator

Again, if you would like to ask a question, please press star then the number one on your telephone keypad.

Our next question comes from the line of Ben Jekic from GMP Securities. Please proceed with your question.

Ben Jekic, GMP Securities

Good morning. Some of the questions have been asked already. I do have two modelling questions, number one on the gross margin expectations for the full year: Does that, the 23 percent to 24 percent range, does that include the benefit of the insurance payment?

Jeff Crystal, Chief Financial Officer

No.

Ben Jekic, GMP Securities

So it's assuming 23.8 in the second quarter?

Jeff Crystal, Chief Financial Officer

Second quarter, yeah.

Greg Yull, Chief Executive Officer

Second quarter, yeah.

Jeff Crystal, Chief Financial Officer

In the second quarter that's what it would be without the insurance, yes.

Ben Jekic, GMP Securities

Okay. Okay. And my second question is on the SG&A. There were some one-time payments made in the quarter. Is that something that you expect to continue or how should we think about SG&A compared to as a percent of your sales?

Jeff Crystal, Chief Financial Officer

So on SG&A, as you see, I mean there's certainly an increase. A good part of that is the variable compensation. So, again, when you look at from quarter one to quarter two, quarter two was quite a strong quarter. So we had some additional accruals in relation to that. But going forward I would say that we would expect these levels to be pretty consistent at this point.

Ben Jekic, GMP Securities

Okay. Thank you.

Operator

Mr. Yull, there are no further questions at this time. I will now turn the call back to you. Please continue with your presentation or closing remarks.

Greg Yull, Chief Executive Officer

Thank you. If there are no further questions I thank you for participating in today's call. We look forward to speaking with you again following the release of our third quarter results in November. Have a good day. Thank you.

Operator

Please note that a replay of this call can be accessed as of 1:00 p.m. today Eastern Standard Time at 1-800-585-8367 until 11:59 p.m. Eastern Time on September 11, 2016. Thank you. You may now disconnect your lines.
