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Chief Executive Officer

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by. Welcome to the Intertape Polymer Group Q1 2020 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.

Joining me from the Company I have Intertape Polymer Group's Chief Executive Officer, Greg Yull, and Chief Financial Officer, Jeff Crystal.

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. You are 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. Please see slide two titled Safe Harbour Statement for further discussion.

During this call we may be referring to certain non-GAAP financial measures as defined under the SEC rules. A reconciliation of the non-GAAP financial measures to the most directly comparable GAAP measures is available on our website at www.itape.com.

Please also note that all dollar amounts are in US dollars unless otherwise noted.

I would like to remind everyone that this conference is being recorded today, May 13, 2020, at 10:00 a.m. Eastern Time.

I will now turn the call over to Greg Yull. Mr. Yull, please go ahead.

Greg Yull, Chief Executive Officer

Thank you and good morning, everyone. Welcome to IPG's 2020 first quarter conference call. Joining me is Jeff Crystal, our CFO.

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

A lot has changed since our fourth quarter call just two months ago. At that point, we were only beginning to recognize the significance of the health and economic challenges facing all of us. We are approaching today's call a little differently than normal, because these are not normal times.

We have increased our level of disclosure to provide as much visibility as possible into where we stand given the COVID-19 pandemic and its impact on the economy and on our business. Coming into this pandemic, our business is much stronger than at any time during which I have led it. I'll outline the reasons behind that in a moment.

The information we are providing today is based on the data available and what we're seeing in the market currently. We are not wearing rose-coloured glasses. On the demand side, we expect the worst could still come or we could be in it right now. But this is equally important: We are not going to be a doomsayer. It serves no purpose for us to speculate. No one knows with certainty the duration of the pandemic or the full impact on the economy.

These are the primary reasons why this morning we've withdrawn our 2020 full-year guidance and replaced it with guidance for the second quarter, which I'll touch on in a moment. What we know today is that the profile of the business, the investments we've made, the diversified portfolio of customer channels and products, as well as the flexibility of our capital structure, place us in a strong position to come out the other side of this situation to compete effectively in the market.

I will touch briefly on the first quarter highlights and then move directly into how we are managing the business through the pandemic. Revenue and adjusted EBITDA were in line with our expectations that we set prior to the outbreak. Revenue was up slightly to $279 million, driven by favourable volume and mix and the acquisition of Nortech. Adjusted EBITDA was $37.5 million, down slightly, just as we cautioned with our guidance at the time of the Q4 call, due mainly to the timing of facility downtime and inventory planning initiatives.

We experienced strong growth in the second half of the quarter in our e-commerce business with both water-activated tape as well as protective packaging. Overall, the demand side held up reasonably well through March despite the shelter-in-place practices introduced across much of North America mid-month, but in the balance of April and now early May, we've seen weaker demand.

Three high-level priorities are guiding how we manage through the pandemic. First and foremost is the health and safety of our employees. Second is protecting our world-class low-cost assets that we have invested in, and this priority is furthered by the delivering on the first priority. Third is protecting our customers by continuing to deliver the essential goods they need from us, which involves working closely with our suppliers to mitigate any potential disruption in our supply chain and to deliver the high level of customer service that we are known for with our customers.

Turning to page four, our first priority, health and safety, has taken on increased importance for everyone. It's a top priority of ours at all times. The culture of safety we've established in our day-to-day operation really pays off in this current situation. A couple of new measures that we've implemented: We are practicing social distancing on the plant floor to protect employees. At times like this, the relatively low labour intensity of our operations is beneficial. Take a look at the photo on the slide. That is a shot of a plant floor taken last year. There are only two people visible on this working line.

Greater attention on our part has been implemented in how employees enter and exit and use common areas. We've also increased the sanitization, disinfectant, and cleaning of equipment and plants to mitigate risks and we have provided protective face coverings to all employees. We believe the measures we've implemented are helping employees feel sufficiently safe to show up to work. We are monitoring absenteeism and while it's up slightly, as one would expect, it is only 10% in North America despite the shelter-in-place practices. At that level, we are not experiencing any impact on our top-line nor any material impact on production. The health and safety of our employees puts us in a great position to protect our assets.

Moving to page five, all of our plants are operational today. We reviewed the various orders and guidelines in the local jurisdictions across our portfolio and, as a result of our products being defined as an essential service, we are operating across the board. We adhered to the shutdown in India announced on March 24th, but each of the four facilities are now deemed essential and have reopened, albeit three at less than 100% capacity. We are truly proud of the fact that our products are essential to our customers and the end users and that we have been able to continue operating our facilities efficiently in the face of this pandemic. This is a testament to all of our hardworking and dedicated employees who come to work every day to make this happen. The breadth of customers and industries we serve bodes well through the whole situation.

Based on your feedback and given the importance of understanding how the pandemic could affect different markets, we are providing our estimates of the diversity of our end markets on page six. This is data that we are presenting for the first time. We do not have access to discrete point-of-sale data, because the vast majority of our sales are through distributors, so this chart is not precise. But in the course of identifying what products should be deemed essential, we gained greater visibility into where our products end up, which gave us additional confidence that these estimates are reasonable approximations of our end market exposures. This represents our estimate for fiscal 2019, not today, nor the impact of the pandemic, but we believe it's helpful to understand the impact of the outbreak on our business.

On the right-hand side of the chart are the verticals that should be growth drivers or stable end markets, specifically the e-commerce growing and food and beverage providing stability. The breakdown on this chart between general manufacturing and transportation appears skewed towards manufacturing, but we believe transportation represents a larger portion and it is difficult to decipher from manufacturing in certain areas. On the right-hand side are the major product categories where we are seeing growth, stability, or demand pressures.

As I mentioned earlier, we have withdrawn our revenue, adjusted EBITDA, and free cash flow guidance for fiscal year 2020 in light of the high level of macroeconomic uncertainty caused by COVID-19. It is simply too difficult to triangulate through the end of the year the duration of the pandemic with the diversity of our end markets, the different puts and takes, and the expected changes in raw material pricing. However, to support visibility into our business and know how it's being impacted by COVID-19 this morning, we provided an interim look at our performance with data available through May the 8th and an outlook for the second quarter. We do not expect to provide quarterly guidance going forward.

We finished March in a strong position, but as we progressed through April, demand changed to show a more unfavourable trend overall. As of May 8th, sales are down 10% compared to the same 38-day period in 2019. Looking forward to the end of the second quarter with the sales data available to date and an order book that stretches two to four weeks forward, we expect revenue to be between $235 million and $250 million and adjusted EBITDA to be between $29 million and $34 million in the second quarter of 2020. The weakness is showing up in volume mix across various products, including industrial tape, films, and carton sealing tapes outside of water-activated.

What we know today is that the real driver of favourability in our business is e-commerce. Our e-commerce customers are running at peak holiday season rates. This is having positive impact not just in our water-activated tape category, but also air pillow systems and mailers. The protective packaging category overall is relatively stable with e-commerce demand offsetting the pressure in other markets we serve.

Our Midland and Menasha assets that produce water-activated tape are operating extremely well. Even before the demand growth from the pandemic, Midland was operating at a level that hit our investment hurdle target for the capital investments on both the initial line and more recently installed second line. This is a great outcome for the business and validation for those investments.

We understand that the extent of the current tailwinds in e-commerce is a direct result of the shelter-in-place practices across North America; however, we believe that the current buying behavior of consumers will positively impact the long-term fundamentals and accelerate the shift of bricks-and-mortars retail to the e-commerce channel. This would only be good news for us, since we would expect to gain disproportionately favourable market share in this shift.

E-commerce is one of our primary growth drivers, tracking our e-commerce customers as they expand in North America and around the world. Our product bundle of tapes and protective packaging and our new offerings that provide sustainability benefits from less waste and greater recyclability put us in a great position to grow in the e-commerce market. As an example, we recently qualified our reinforced water-activated tape as recyclable, which expands on the sustainability progress we announced earlier this year.

We are also experiencing new business from our wovens application directly related to the pandemic. Sites are using wovens as shelter for testing locations and healthcare-related service. In addition, as part of our commitment to support our healthcare workers, we are providing woven material for surgical gowns as part of the buildup of PP&E.

On the other side of the demand curve in the current environment are general manufacturing, building construction, transportation, and retail. Based on the current order patterns, it is difficult to unpack the negative impact on demand in these end markets versus the effect of de-inventorying at the distributors, which we are aware is happening. We saw similar situations in 2008, 2009, as well as in the fourth quarter of 2015 on films when oil prices fell. In each of those cases, once distributors worked through their inventory, order patterns rebounded, and in this case that would give us a clear view of demand in those end markets. We've seen some early signs that distributors may have worked through their inventory in certain carton sealing tapes and films, but it's still too short of a period at this stage to draw definitive conclusions.

In the face of this situation, we are highly sensitized to cash management, protecting our cash just like we protect our hard assets. We are implementing measures to mitigate costs and have a flexibility in certain aspects in the near term as it relates to non-essential or new projects, a companywide salary position hiring freeze, the postponement of annual pay increases for salaried staff, and suspension of business travel and entertainment. In March we also announced the reduction of our CapEx range to $30 million to $40 million in fiscal 2020, which provides us with additional flexibility. We will continue to respond accordingly on the cost side on a go-forward basis depending on the depth and duration of the economic downturn.

On the production side, all facilities continue to operate, but we have flexed and will continue to flex capacity on specific lines to ensure production is aligned with demand

and we are not building inventory. This is especially true given the recent price pressure in oil. We are not seeing yet the same pressure in our raw materials, but it's fair to expect in over the coming months. We are extremely cognizant of inventory levels in a falling raw material environment. The investments and the acquisitions we've made over the past four years have strengthened our product bundle and provided a world-class, low-cost manufacturing asset base that can compete efficiently through market cycles.

The nature of the pandemic and the actions taken to prevent a greater crisis are unparalleled. We are appropriately cautious, but also confident that how we enter this situation positions us to weather it and come out strong on the other side.

With that, I'll turn it over to Jeff to review the financials. Jeff?

Jeff Crystal, Chief Financial Officer

Thank you, Greg.

On page nine of the presentation we present an analysis of our revenue for the first quarter. Revenue increased 0.4% to $278.9 million compared to the same period in 2019. The increase was primarily due to a $2.3 million improvement in volume and mix and a $2 million increase from the Nortech acquisition in February that we discussed on the fourth quarter call. These improvements were partially offset by price, which was a $2.7 million headwind, driven mainly by decreases in raw material input prices. The positive drivers within volume and mix in the quarter were water-activated tape and protective packaging with pressure coming from certain carton sealing tapes as well as industrial tapes.

Turning to page 10, gross margin was up 32 basis points to 21.1% in the first quarter compared to the same period in 2019. The improvement in margin from the first quarter of 2019 is primarily due to the increase in spread between selling prices and combined raw materials and freight costs, which was partially offset by an increase in costs related to the inventory planning initiatives we mentioned on the fourth quarter call.

Looking at the profile of our cost base, the nature of our business is skewed to the variable cost side versus fixed costs, which is a significant benefit in the face of the pandemic. Raw materials are our most significant costs, which are variable, accounting for approximately 60% of our cost of sales. Approximately 6% to 7% of the cost of sales is freight, another variable. Direct labour is relatively low from a manufacturing standpoint at only about 6% and the remainder is overhead, which has both a fixed and variable component. So, from a cost perspective, we believe we have the appropriate levers to flex production as appropriate, as Greg referenced earlier.

Adjusted EBITDA was $37.5 million or $0.8 million lower than the same period last year. This decrease is mainly driven by the increase in SG&A in 2020, excluding the favourable effect of the stock-based compensation benefit, which resulted from the net impact of an increase in salary-related costs that were largely offset by a decrease in variable compensation and reductions in anticipated discretionary defined contribution plan contributions.

Cash flows from operating activities improved by $2.4 million to an outflow of $16.1 million in the first quarter compared to the same period in 2019. The improvement was primarily the result of a decrease in cash used for working capital items and an increase in gross profit. These increases were largely offset by an increase in federal income taxes paid.

Turning to page 11, in a normal environment the business has a natural seasonality in working capital as we build inventory in the first half of the year in advance of both the higher volume third and fourth quarter periods from a retail activity perspective, as well as our planned factory maintenance schedule, which occurs primarily at mid-year. In the fourth quarter that build unravels with the seasonal nature of higher retail activity. In the context of COVID-19, that trend should remain true in the second quarter, but depending on the duration of the pandemic, the build in the second half of the year is not known at this point.

Free cash flows improved by $12.8 million to negative $23.5 million in the quarter compared to the same period in 2019, primarily due to a decrease in capital expenditures. Given the natural seasonality of the business, we expect negative free cash flows in the first quarter and then to progressively build more positive cash flows through the course of a normal year, as I mentioned earlier.

In the current environment, liquidity and the capital structure are critical to durability. We entered the pandemic in a strong position in each case. We finished the first quarter with $329.1 million in cash and loan availability. Our secured net leverage ratio, which is our most important loan covenant, was 1.8 times, well within its limit of 3.7 times. The ratio ticked up slightly by four-tenths of a turn in the quarter due to the Nortech acquisition and the normal seasonality of our working capital that I mentioned earlier.

From a capital structure perspective, the $250 million of senior unsecured notes issued in October of 2018 is critical to the flexibility we have today. The unsecured offering provides greater flexibility on the key secured net leverage ratio covenant, which significantly de-risks the balance sheet. Basically, the $250 million of unsecured notes is not included in our secured leverage covenant calculation. Based on feedback from analysts and some investors, most feel this is not well understood broadly, so we will keep driving this point home for folks.

Our total leverage ratio at the end of the first quarter, including the unsecured debt came, in at 3.4 times, moving in line with the Nortech acquisition and the working capital seasonality I referenced. We do not have any maintenance covenant on total leverage, so this does not put us at any risk under our credit agreements. Again, it is our secured net leverage ratio covenant of 1.8 times that is measured versus our limit of 3.7 times.

As Greg mentioned earlier, we are managing cash to preserve our priorities of debt repayment and maintaining the dividend. We entered this downturn in a much stronger position than was the case in 2008. The 20%-plus margins we are running today are about double where we were in 2008. At these levels, it provides us a much greater degree of flexibility and buffer compared to where the business was then, so we feel very confident from that perspective on a relative basis.

Our market share in e-commerce provides greater diversity in terms of customers, end markets, and favourable buying behaviour through this pandemic, and with our strategic CapEx program completed, we were able to reduce our CapEx spend this year, having already made significant investments to increase scale and improve efficiencies.

With the onset of the COVID-19 pandemic and the uncertainty of its duration, we are announcing this morning that we are not actively pursuing any acquisitions until such time that the outlook for the economy stabilizes. There is simply too great a risk to accurately model a company's future EBITDA and cash flow metrics at this stage. Once the economy stabilizes, we believe the flexibility of our capital structure, the strong financial position in which we entered this situation, the scale of our business, and our ability to consolidate targets and generate cost synergies will provide opportunistic acquisitions.

As a result of putting our M&A strategy on pause and the uncertainty as to the depth and length of the current macroeconomic downturn, we have decided to remove the 2022 targets for revenue and adjusted EBITDA today. The 2022 targets were established in 2016. At that point, the business was significantly smaller, generating approximately $780 million in revenue and a little over $100 million in adjusted EBITDA. As we have consistently highlighted, successfully achieving the 2022 targets required several additional acquisitions. We have always strived to maintain our commitment to be disciplined and not overpay for acquisitions to achieve targets that were based on a certain level of M&A activity in a very different economic environment. As such, we believe it is appropriate to withdraw those 2022 targets.

Now I'll turn it back over to Greg for his closing thoughts. Greg?

Greg Yull, Chief Executive Officer

Thanks, Jeff.

Prior to the pandemic, we'd implemented a series of measures to position us for success. We completed $160 million plus capital investment program in 2017 and 2018. We acquired businesses that strengthened our product bundle and expanded our customer base. We've improved our margin profile through disciplined management of the spread between the selling price and the cost of raw materials. We restructured our capital stack with a bond offering in 2018 that Jeff mentioned, specifically to improve our financial flexibility in the event of a downturn. We increased our dividend last year and we remain committed to that level of dividend, providing comfort to our investors.

We supply essential products to a diverse range of customers and end markets and our packaging tapes and protective solutions offer out-sized exposure to e-commerce growth and the shift in retail behaviour. These are the essential characteristics that position us to come out the other side of this pandemic in a strong position in the market.

Before closing, I'd like to thank all of our employees. This is a very challenging situation for everyone. I could not be more proud of how they've conducted themselves and the level of commitment to the organization they have demonstrated. It's truly tremendous.

With that, I'll turn the call back to the operator and open up the question-and-answer period. Thank you.

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 two-tone prompt to acknowledge your request. If your question has been answered or you wish to withdraw your registration, please press the pound sign 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.

First question comes from the line of Michael Doumet with Scotiabank. Please proceed with your question.

Michael Doumet, Scotiabank

Hey. Good morning, guys. So I'm going to start off just by trying to square off the Q2 revenue guide, which implies an 18% revenue decline at the midpoint on a year-over-year basis. I'm trying to square that off with your comment that the company sales through May 8th declined 10%. I mean does the steeper decline in the second half of Q2, does that, in your opinion, reflect the destocking from distributors? And what does that mean for Q3?

Greg Yull, Chief Executive Officer

Well, listen, we're not going to be predicting kind of Q3, but certainly what we're seeing right now and what we've seen historically in environments of a downturn or even a downturn in oil is we've seen destocking happen at the inventory level. At some point, typically or historically, consumption demand lines up with our demand, but there's a period of time where our demand is lower than the actual consumption demand happening in industry. Hard to predict when that happens. I mean typically it usually takes about a quarter to kind of work through and right-size that inventory so that you line up more to consumption demand. But we've seen that historically and it's hard to articulate or to know for sure what amount of de-inventorying is happening.

Michael Doumet, Scotiabank

Okay. But Greg, just to be clear, I mean you did comment that you saw early signs that distributors were finishing or that you were seeing less destocking for your distributors.

Greg Yull, Chief Executive Officer

Yeah. I mean, look, we've seen, in a finite period of time, I mean a couple of days, a week, we've seen some pickup, but I'm not going to call that that's going to continue for the quarter and move forward. It's just, it's too unpredictable.

Michael Doumet, Scotiabank

No, fair enough. Very uncertain times. So, maybe just taking it into your (inaudible) guide, the midpoint implies a 200 basis points margin compression. I wanted to get your sense on whether the bulk of that you were expecting from either lower gross margins or lower overhead absorption. I mean are you finding that you are at least able to maintain your gross margin dollar in this environment?

Jeff Crystal, Chief Financial Officer

Yeah. I mean certainly we're going to come under pressure in Q2, like you mentioned, about lower overhead absorption, so we're trying to flex our plants to match up with the demand that we're seeing. And the unfortunate impact of that, of course, is you have less absorption of your fixed costs and that does hit your P&L. So there will be an impact of that certainly in Q2. So, from a cash flow perspective, that's not necessarily an impact, because we would have incurred those costs anyway, but certainly from a P&L perspective you have that hitting.

Michael Doumet, Scotiabank

Okay. And maybe just flipping to the dividend here, the initial 2020 guide implies that the dividend would be twice covered by free cash flow. Now lower sales and lower resin prices should reduce the working capital requirement through the year. I mean what's your comfort level as it relates to being able to fund the dividend through free cash flow generation in 2020?

Greg Yull, Chief Executive Officer

So, as I mentioned in my prepared remarks, we're comfortable where we are right now. The board reviews it every quarter and, with what we know right now, we're comfortable with where that dividend is and plan to keep that in place. I mean we don't know, like anyone else, we don't know what the future holds. We don't know Q3, Q4. I mean when you think about it, you could apply some logic to it that says that the shutdowns could have a more dramatic impact on Q2 and you could make an assumption that, with a lot of businesses starting up into phase one, at least in North America, that you should see some demand increase. But again, those are just thoughts that I have on a go-forward basis.

Michael Doumet, Scotiabank

I think they line up with my thoughts as well. But look, Greg, appreciate the comments. Good luck. Thank you.

Greg Yull, Chief Executive Officer

Thanks, Michael.

Operator

Your next question comes from Daryl Young with TD Securities. Please go ahead with your question.

Daryl Young, TD Securities

Good morning, guys. My question is around the e-commerce side and I guess, I mean it's proving to be very attractive and a good investment strategy previously. Just wondering if you're seeing any entrance of new competitors or anyone moving into that space or talks of that currently just given how well it's been going.

Greg Yull, Chief Executive Officer

No. We have not had any insight on that or heard anything about that.

Daryl Young, TD Securities

Okay. And then do you have a sense of the magnitude of the cost savings from the fall in oil prices and resin prices currently?

Greg Yull, Chief Executive Officer

Yeah, really hard to predict. So, when you think of some of the bigger buys on the resin side, basically we sit here so far this year and we're flat because there was an increase that went through in the beginning of the year and that increase has come down in the last, I don't remember the exact date, but certainly in the last 30 days. So we're basically flat. As I mentioned in my remarks, fair to assume that you're going to see some falling raw material prices, both as input costs drop or feedstock costs drop and also demand wanes, but we don't have any order of magnitude right now. It's actually been surprisingly stable for the most part.

Daryl Young, TD Securities

Okay. That's it for me. Thanks.

Operator

Next question comes from Stephen MacLeod with BMO Capital Markets. Please proceed with your question.

Stephen MacLeod, BMO Capital Markets

Thank you. Good morning, guys.

Jeff Crystal, Chief Financial Officer

Good morning.

Stephen MacLeod, BMO Capital Markets

Good morning. I just had a couple of questions. You gave some good colour around the end market breakdown, so thank you for giving that colour. Can you talk a little bit about what markets outside of e-commerce and food and beverage, like where you're seeing above or below average demand declines?

Jeff Crystal, Chief Financial Officer

Yes. So I mean I would say that in like the transportation, like we expected, I mean we're certainly seeing a lot of pressure there. As you know, certain plants shut down, the industry's shut down. I would say on the building and construction, there it's been somewhat mixed, because we've had certainly declines in certain areas, but like we've said in our wovens business, which has probably the highest percentage of building and construction out of our portfolio, we've had some upside related to the temporary structures, so structure fabric to be basically temporary tents for testing facilities or temporary hospitals and things like that. So we've seen an uptick there.

We've also seen an uptick in volume related to material going into making surgical gowns. That's specifically in Canada. So we're actually selling to several textile or clothing companies that are manufacturing these gowns for the government and for the medical and healthcare industry. So we've sort of seen a mixed bag there. Even on the retail side, it's certainly been under pressure, but we've also seen some mixed bag there too with some order patterns that look quite positive at times and somewhat negative at other times. But I would say that outside of e-commerce and food and beverage, certainly there's more pressure in a general sense.

Greg Yull, Chief Executive Officer

And just to add onto that, I mean you just think of, in the transportation segment, we have a fair amount of product going out of our protective packaging business into transportation. That was shut down and has been shut down. In the midst of starting up right now. Certainly, we've got a pocket of aerospace that basically was shut down. I don't know what the recovery rate is going to be there, probably pretty low. But certainly we've seen some pockets of just pure shutdowns on that side. And again, we do see pockets of strength in certain building construction products and some channels but, as Jeff said, it's a mixed bag.

Stephen MacLeod, BMO Capital Markets

Okay. That's helpful. Thank you. Maybe just expanding on that, within transportation, how much of it goes into the aerospace business versus automotive or other end markets? Or is that too granular?

Greg Yull, Chief Executive Officer

The aerospace market would not be a significant portion of that.

Jeff Crystal, Chief Financial Officer

Automotive would be much larger.

Stephen MacLeod, BMO Capital Markets

Okay. And are you seeing automotive demand begin to pick up as plants open back up? Or is that too soon?

Greg Yull, Chief Executive Officer

Too soon.

Stephen MacLeod, BMO Capital Markets

Okay. That's fine. And then maybe just as you think about the cadence through the year Q2, Q3, Q4, and given the fact that uncertainty sort of runs high, but would you expect Q2 to potentially be a trough in terms of year-over-year declines? Like do you see in your order book or from distributors any indication that there would be a pickup in demand on a relative basis through the back half of the year?

Greg Yull, Chief Executive Officer

I mean, look, that's the question that everyone is struggling with, right? Certainly if you look at bank forecasts, you would expect that on a go-forward basis, but in our perspective it's too early to call.

Jeff Crystal, Chief Financial Officer

I think, like we said, we're not going to make those predictions, but what we see now, certainly with the stay-at-home orders being lifted to some degree, again, nobody knows whether that's going to generate a ton of more infections and you're going to have a double dip, but at the same time, in the near term, we expect that to be positive, because there's things that are shut down that won't be in the near term. So that would be certainly a net positive.

But again, and then there's the de-inventorying effect, which we discussed earlier, which again, we don't know what that's really going to look like and the timing of that, but that could be a net positive as well that could come. But again, we're not going to predict whether it's the trough or not at this point.

Stephen MacLeod, BMO Capital Markets

Okay. And then you gave some colour around fixed versus variable on cost of goods sold. Are you able to give some colour for SG&A?

Jeff Crystal, Chief Financial Officer

We haven't given that colour in SG&A. I would say, I mean the majority of SG&A would be fixed. There are some variable components in there. Certainly the variable compensation, which we don't break out, but there's variable compensation in there. There's also sales-related costs like commissions, internal and external, which would be variable. So there is definitely a variable component within there, but I would say the majority would still be a fixed cost.

Stephen MacLeod, BMO Capital Markets

Okay. That's great. Thank you very much. That's it for me.

Operator

Next question comes from Walter Spracklin with RBC Capital Markets. Please proceed with your question.

Ryall Stroud, RBC Capital Markets

Hi. Good morning, everyone. This is Ryall Stroud calling in for Walter Spracklin at RBC. Thanks for taking my question. I just wanted to touch on e-commerce quickly. Was curious on getting your thoughts on how significant the impact of e-commerce has been since the pandemic began and maybe if you're able to quantify what that benefit looked like towards the end of the quarter and into May.

Jeff Crystal, Chief Financial Officer

So, we aren't open to quantifying that at this point, but what we can say is that e-commerce has been, like Greg said in his prepared remarks, has been just operating at peak levels. So we've seen certainly the large customers like Amazon operating like they are operating at peak. We've seen massive increases in volume coming from other e-commerce providers, such as Wal-Mart and Target. So, no question at peak and, like we said, that's affecting several product lines, so not only our water-activated tape but we've seen our air pillow systems as well as mailers just knocking the lights out.

Ryall Stroud, RBC Capital Markets

Okay. That's really helpful. And then with leverage looking to tick a bit higher here in the quarter and M&A now being put on hold it seems, where do your capital allocation priorities currently lie and do you expect that that free cash flow generation going forward would be primarily redirected towards debt repayment until kind of visibility on M&A improves?

Greg Yull, Chief Executive Officer

Yeah. I mean our priority before this was debt repayment and it certainly still is debt repayment. And as we said, with M&A being shut down, debt is the option.

Ryall Stroud, RBC Capital Markets

Okay. Then just one last one for me: We saw pricing acted as a bit of a headwind in the quarter. Is this a trend that you're seeing in May as well? And then in terms of what's been causing this pressure, have you seen customers starting to look for concessions? Or have you seen competitors start to lower prices to try to attract volume? Just kind of curious getting some colour there.

Greg Yull, Chief Executive Officer

Sorry, we missed the beginning of your question. Was it around pricing?

Ryall Stroud, RBC Capital Markets

Yes. So, with pricing acting as a headwind in the quarter, just curious what caused that, if it's been competitors starting to lower prices to attract volumes or customers looking for concessions.

Jeff Crystal, Chief Financial Officer

Yes. And that was driven really by raw material decreases, primarily in polyethylene, but really over the back half of last year into this year, so that's something that was expected. And again, when we manage that, we always managed to the spread. We always try to make sure we protect the spread between sell price and raw materials and freight.

So, for us, certainly we expect it to give up some of that as the lower raw material environment persisted. But that was really just normal pressure from customers, normal competitive pressures. Again, the market is very disciplined. Nothing related to what's going on now. And we're not really seeing any impact or any change in the way competitors are behaving based on what's happening now.

Ryall Stroud, RBC Capital Markets

Okay. That's great. Thanks a lot. I'll pass the line.

Jeff Crystal, Chief Financial Officer

Okay. No problem.

Operator

The next question comes from Neil Linsdell with Industrial Alliance. Please proceed with your question.

Neil Linsdell, Industrial Alliance Securities

Good morning. Just two quick things here. I know you don't have a lot of point-of-sale visibility, but are you seeing any kind of trends or any kind of insight into geographic impacts on your sales or benefits?

Greg Yull, Chief Executive Officer

Well, certainly from an impact perspective, when we look at our business in the northeast of the US, certainly that has been hurt more than other parts of the country. So I would say it would follow the intensity of COVID-19. The higher intensity of COVID-19 in an area, the lower the sales have been. So certainly west coast, east coast, but outside of that it's hard to get any more granular than that.

Neil Linsdell, Industrial Alliance Securities

And you mentioned on the raw materials pricing but have you had any supply chain issues as far as or concerns about getting raw materials or goods or anything that's critical in your manufacture?

Greg Yull, Chief Executive Officer

We have been very fortunate in our ability to keep our supply chains intact from a raw material perspective. And certainly we had issues over the past nine weeks and we've worked our way through it, so everything is intact as of right now.

Neil Linsdell, Industrial Alliance Securities

All right. That's it for me. Thanks.

Operator

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

Greg Yull, Chief Executive Officer

Thank you for participating in today's call. We look forward to speaking with you again following the release of our second quarter 2020 results in August. In the meantime, I hope you and your families are safe and healthy. Thank you.

Operator

Please note that a replay of this call can be accessed as of 1:00 p.m. today, Eastern Daylight Time, by dialing 1-800-585-8367 within North America and 1-416-621-4642 for international callers. You may now disconnect your lines.

Operator

This concludes today's conference call. You may now disconnect.
