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Conference Call Transcript

RS - Q2 2009 Reliance Steel & Aluminum Co. Earnings Conference Call

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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to Reliance Steel & Aluminum 2009 Q2 financial results conference call. (Operator Instructions). It is now my pleasure to turn the floor over to your host, Mr. David Hannah, Chairman and CEO. Sir, the floor is yours.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

Good morning and thank you for taking the time to listen to our conference call for the second quarter and six months ended June 30, 2009. Gregg Mollins, our President and Chief Operating Officer, and Karla Lewis, our Executive Vice President and Chief Financial Officer are also here with me today. After the completion of this conference call a printed transcript including Regulation G Reconciliations will be posted on our website at: www.rsac.com/investorinformation.

I must say that it does hurt some to report our second quarter numbers. We are surely disappointed with the operating results, but I am not disappointed with the efforts and commitment of all of our employees. We did make the best out of a very very difficult operating environment, the most challenging we have ever seen.

Most all of the industry analysts have written about the sharp drop in carbon steel prices during the second quarter, to levels lower than expected, so we should not be too surprised by the results. As prices continued to decline during the quarter, metal service centers, including us, increased "destocking" activities, which led to lower FIFO gross profit levels. In addition to the challenges of the pricing environment, demand continued

to soften throughout the quarter, dropping on an average daily basis about two to three percent per month. Overall, compared to the 2009 first quarter, our tons sold were down 7% and our average price per ton sold was down 14%.

All of this led to a net loss (our first since 1975) of \$5.8 million, or \$.08 per diluted share for the 2009 second quarter, compared to net income of \$156.6 million, or \$2.12 per diluted share for the 2008 second quarter, and net income of \$20.1 million, or \$.27 per diluted share, for the 2009 first quarter. Sales for the 2009 second quarter were \$1.2 billion, down 41% compared with 2008 second quarter sales of \$2.1 billion, and down 20% from the 2009 first quarter.

For the six months ended June 30, 2009, we remained profitable with net income of \$14.3 million, compared with net income of \$264 million for the same period in 2008. Earnings per diluted share were \$.19 for the six months ended June 30, 2009, compared with earnings of \$3.58 per diluted share for the six months ended June 30, 2008. Sales for the 2009 year-to-date period were \$2.8 billion, compared with first half 2008 sales of \$4.0 billion.

For the 2009 second quarter, carbon steel sales were 57% of our revenues; aluminum sales were 19%; stainless steel sales were 12%; alloy sales were 6%; toll processing sales were 2%; and other sales were 4%. In total, we sold about 873,000 tons of metal during the 2009 second quarter. By major product group, we sold 740,000 tons of carbon steel products during the 2009 second quarter, which was down about 7% from the prior quarter, with average selling prices down about 17%. Aluminum sales were 46,000 tons, which was down 3% from the previous quarter, with average prices down 8%. Stainless steel sales were about 40,000 tons, down 4% from the prior quarter and prices were down 13%. Alloy sales were 31,000 tons, down 26% with prices down 4%.

As you can see from these comparisons, nothing was spared. Business was difficult across all of our products. The largest percentage price decrease was in carbon steel products as the mills continued to lower their prices to unexpected levels. The largest percentage drop in tons sold was in alloy sales, caused mainly by the softening in the energy and oil and gas industries. Those industries though, along with aerospace, were still our best performing ones.

We told you at the end of the previous two quarters that we would focus our efforts on maintaining profitability, maximizing cash flow through working capital management, debt reduction, and expense control. We are somewhat satisfied that we were able to maintain our profitability for the first-half of the year in this very difficult environment but, again, upset with the second quarter's results. We are proud of our cash flow from operations of \$367 million in the second quarter and \$681 million for the first-half of 2009, resulting mostly from reductions in inventory and accounts receivable balances. We have also been attacking our operating expenses where, on a same store basis for the first-half of 2009, our Warehouse and S,G & A expenses are down \$138 million, or 24%, compared to the 2008 first-half. Also during the 2009 second quarter we repaid \$194 million of debt and had accumulated about \$180 million of cash as of June 30, 2009. Our \$1.1 billion revolving credit facility has no outstanding balance and our net debt-to-total capital ratio decreased to 30.7% at June 30th.

Once again, I commend our managers and their teams for their skillful execution during these most challenging times. They have done what we expected them to do and as a result we are in a very sound financial position at just the right time. There is some good news in that we do feel the worst is now behind us, despite our belief that there will be no meaningful improvement in real demand through the balance of this year. We have seen some spotty improvement in demand in the auto and appliance areas, as well as in bridges and barges, schools and hospitals and the defense-related aerospace business is still okay. Quoting activity seems to have picked up, but there has not been a related pick up in actual orders, at least not yet. There was also no meaningful amount of "stimulus" spending, as best as we could tell.

We saw a small improvement in May of 2009 in our FIFO gross profit margins, the first sequential monthly increase since last May of 2008, and a more meaningful improvement in June, which represented the highest monthly level we have seen so far this year. These improvements are the result of the recent price increases for most all of our products, as well as a better inventory position with more current costs. We expect this trend to continue through the 2009 third quarter given the announced price increases. Our tons in inventory at June 30, 2009 represented 2.6 months on hand based on June sales volumes. We do expect our gross profit margins to improve in the third quarter over the second quarter because of the mill price increases, as well as our inventory being in better balance with current business levels. There are still some areas where we will be decreasing inventory but not at the same rate or cost as we did during the first-half of the year. We are now focused more on making some money and less on cash flow.

Demand, however, is a different story. The rate of decrease in shipments on an average daily basis slowed during May and June, but it was still down more than we projected. There remains a good deal of uncertainty, still, regarding economic conditions, and the timing of any improvement in real demand. While we expect the third quarter to be a return to profitability, we are not comfortable providing third quarter 2009 earnings guidance at this time. We will, as the quarter progresses, communicate any meaningful information regarding our operations as it becomes available.

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On July 22, 2009, the Board of Directors declared a regular quarterly cash dividend of \$.10 per share of common stock. The dividend is payable on September 14, 2009 to shareholders of record August 21, 2009. The Company has paid regular quarterly dividends for 49 consecutive years.

In closing, we are still in difficult economic times, but pricing has improved and demand seems to be near the bottom. Our inventories are in a much better position. We have generated more cash from operations in the first-half of 2009 than in any other full-year period, and our debt has been reduced significantly with our net debt-to-capital near historic lows since we became a public company 15 years ago. Additionally, operating expense levels have decreased materially in response to the decline in business activity. We have done what we intended to do to manage successfully through this recessionary period, to position ourselves well for the eventual recovery, and to take advantage of any attractive opportunities for future profitable growth. Thank you. I will now turn the call over to Gregg for some additional comments on our operations and market conditions. Gregg?

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

Thank you, Dave and Good Morning. Obviously all of us are very disappointed in our results in the second quarter. Frankly, we did not expect prices on all of our products to dip as low as they did and for demand to follow suit. However, I am extremely proud of how our managers quickly reacted to the challenges they faced throughout the quarter. When the going gets tough the tough get going and that is exactly what they did. We continued to reduce our inventories both through customer sales as well as inter-company transfers. We took \$346 million dollars out of inventory in the second quarter as service centers, including ourselves, continued destocking. This helped our cash flow but had a negative affect on our gross margins.

We continued our efforts to reduce costs by cutting our personnel by 6% in the 2009 second quarter, 14% in the 2009 first-half and 21% from September of 2008. Bottom line, we reduced our work force by 2,300 over the last nine months. In addition, we reduced the number of hours worked, offered work furloughs and froze salaries in most of our locations, all in an effort to maintain profitability. Unfortunately, metal prices and demand dropped faster than we could reduce our costs.

Managing gross profit margins was by far our biggest challenge in the quarter. Massive de-stocking and liquidation of inventory took place throughout the quarter particularly in carbon products. This resulted in our FIFO margins dropping from 17.9% in the 2009 first quarter to 16.7% in the second quarter. It doesn't get much uglier than that. Going forward, we believe end use demand has hit, or is at least near the bottom and we expect some modest improvement in the second-half of 2009 as our customers re-stock their inventories. We have seen an increase in quoting activity, which is encouraging, and we believe this will ultimately have a positive impact on our volumes.

Aerospace, especially military and defense, has done quite well. We have seen an increase in activity in the semiconductor industry recently as well as barge and ship building and heavy equipment. We also believe the future for energy related projects is good, held back only by the financial markets. As for pricing, carbon flat-rolled will be up over \$100 a ton in September compared to June. Price increases on beams, mini-mill products, plate and tube are all holding. Due to the reduction of production capacity initiated by the producers, lead times are rapidly moving out. This is bringing stability to the market and buyers back to the table.

As for aluminum, Midwest spot ingot is in the upper \$.70 a pound range which is more than \$.10 a pound higher than in April of 2009. Heat-treat plate, that supports the aerospace industry, is readily available mainly due to lower build rates than planned and prices have come down quite a bit since the first of 2009. Lead times on most products are six to eight weeks. Stainless prices have also risen both on published base prices as well as the surcharge. Base prices are up 12% in August compared to April and the surcharge is up over \$.20 a pound over the same period. Here again production lead times are six to eight weeks.

So in closing, it is a difficult market to read. There are some signs that would normally indicate an upside in volume – but these are not normal times. Price increase announcements are the best news we have had in some time. De-stocking has slowed down and gross margins should improve. We shall see. Now I will turn the program over to Karla to review the financials.

Karla Lewis - Reliance Steel & Aluminum Co. - EVP & CFO

In the 2009 second quarter, our tons sold decreased 7.4% from the 2008 second quarter and 7.3% from our 2009 first quarter. However, in August 2008 we purchased the PNA Group of companies, our largest acquisition to-date based on transaction value. On a same-store basis, which excludes our 2008 acquisitions, our 2009 second quarter sales were \$990.7 million, with our tons sold down 38.8% from the 2008 second quarter and down 8.7% from the 2009 first quarter. Our average selling price per ton sold in the 2009 second quarter was down 34.8% compared to the 2008 second quarter. On a same-store basis, our 2009 second quarter average selling price was down 21.2% from the 2008 second quarter.

Our 2009 first half sales of \$2.8 billion were down 30.0% from our record 2008 first half sales of \$4.0 billion. This includes a 4.3% decrease in tons sold and a 25.6% decrease in our average selling price per ton sold. On a same-store basis, our tons sold were down 36.3% and our average selling price was down 10.9%. According to MSCI data, tons sold for the 2009 first half were down about 44% for the industry compared to the 2008 first half.

Our average selling price declined mainly because of the significant cost reductions for most products that we sell. Our largest product groups are carbon steel structurals and plate, that combined made up 26% of our 2009 second quarter sales. The most significant mill price declines for these products occurred early in the 2009 second quarter and prices continued to fall further than we had anticipated, significantly impacting our average selling prices and gross profit margins. Our 2009 product mix also contributed to our lower average selling prices with carbon steel products, which typically sell at lower prices than most other products that we sell, representing 57% of our 2009 second quarter sales compared to 51% of our 2008 second quarter sales mainly due to our August 2008 acquisition of the PNA Group.

Our 2009 gross profit margins have been significantly reduced because of the lower demand and pricing levels just discussed. Our 2009 second quarter gross profit margin was 22.8%, compared to 28.0% in the 2008 second quarter and 22.7% in the 2009 first quarter. For the 2009 first half, our gross profit margin was 22.7%, compared to 27.0% in 2008. Because our customer demand fell so significantly and so rapidly at the same time that replacement cost for our products was falling, our FIFO inventory costs on hand were generally higher than current replacement cost. Also, with the reduced customer demand levels, we cut back our purchasing activity which delayed the impact of the lower replacement costs on our average inventory cost.

In the 2008 second quarter we were experiencing somewhat higher gross profit margins than our historical average because as our suppliers announced price increases we pushed these increases through to our customers before we received the higher cost metal into our inventory. This resulted in a temporary improvement in our gross profit margins.

Because of the significant decline in our inventory costs in 2009, especially for carbon steel products, we recorded a LIFO adjustment in the 2009 second quarter that was a credit, or income, of \$75.0 million, compared to LIFO expense of \$40.0 million in the 2008 second quarter. In the 2009 first half we recorded a LIFO credit, or income, of \$150.0 million, compared to LIFO expense of \$57.5 million in the 2008 first half. Our current estimate for our 2009 annual LIFO adjustment is a credit, or income, of \$300.0 million consistent with our view for the 2009 first quarter. Our LIFO adjustment is included in cost of sales.

Because of the significant decline in business activity levels, we have been aggressively reducing our warehouse, delivery, selling, general and administrative expenses. Our 2009 second quarter expenses are down \$49.7 million, or 17%, compared to our 2008 second quarter expenses. On a same-store basis, our 2009 second quarter expenses are down \$90.0 million, or 30%, compared to the 2008 second quarter. Our 2009 second quarter expenses were 19.9% of sales, compared to 14.2% in the 2008 second quarter.

Our cost structure is highly variable, with about 60% of our expenses personnel-related. In the 2009 first half, we reduced our headcount by just under 1,500, or 14%, with a reduction of about 550 in the 2009 second quarter. Since September 30, 2008, we have reduced our headcount by 2,340, or 21%. In addition to the headcount reductions, we have several employees working reduced hours resulting in additional savings. Further, throughout our workforce, employees have a significant portion of compensation tied to profitability. Because of the lower profitability levels in 2009 our compensation expense has declined. Our expenses for the 2009 first half also include \$11.4 million related to potentially uncollectible accounts receivable, an increase of \$4.5 million from the 2008 first half. Our 2009 expenses as a percent of sales have also increased substantially because of the lower selling prices compared to 2008. We will continue to closely monitor our expense levels and take further action if warranted.

Our 2009 first half depreciation and amortization expense of \$59.4 million increased 39% over 2008 mainly due to our 2008 acquisition of the PNA Group and from our capital expenditures made since June 2008. Our operating income for the 2009 first half was \$53.4 million, or 1.9% of sales, compared to \$457.2 million, or 11.4%, in the 2008 first half. The lower sales volume levels combined with our compressed gross profit margins in 2009 have significantly reduced our operating income.

Interest expense for the 2009 first half of \$36.0 million increased 10% compared to 2008 mainly because of our increased borrowings for the \$1.1 billion purchase of the PNA Group in August 2008. Comparing the 2009 second quarter to the 2009 first quarter, our interest expense decreased \$2.6 million because of the significant debt paydowns made during the quarter. Because we incurred a pre-tax loss in the 2009 second quarter, we realized an income tax benefit of \$3.9 million. Our effective income tax rate for the 2009 first half was 29.8% compared to 37.7% in the 2008 periods.

In the 2009 second quarter, we continued to significantly reduce our working capital and generated \$366.7 million of cash flow from operations. For the 2009 first half, we generated \$681.3 million of cash flow from operations compared to \$128.4 million in the 2008 first half. Our accounts receivable balance decreased \$291.8 million, our inventory levels decreased \$470.2 million, and our accounts payable and accrued expenses decreased \$151.5 million.

Our average accounts receivable days sales outstanding rate at June 30, 2009 was about 43-1/2 days compared to 42 days at December 31, 2008, and 43 days at March 31, 2009. Our DSO rate has trended up as sales have decreased and we have seen some of our customers pay us more slowly. In the 2009 first half, we wrote-off \$10.8 million of customer receivables as uncollectible. Our full year 2008 write-offs were \$8.1 million. Our allowance for uncollectible accounts at June 30, 2009 was \$22.7 million. Although we anticipate some further receivable write-offs, we believe that our allowance is adequate to absorb any such losses. Our customer base is very diverse and our largest single receivable balance at June 30, 2009 was less than \$6.5 million and we only have eleven accounts with a balance greater than \$2 million.

Our inventory turn rate for the 2009 second quarter and first half was 3.4 times compared to 3.9 times in 2008. Because customer demand fell off so dramatically and has continued to fall, we have not been able to reduce our inventory faster than our shipments have decreased. As of June 30, 2009, our inventory tons on hand were down 32%, and our FIFO inventory balance was down 37% from December 31, 2008. Our inventory turns have also declined somewhat because of our 2008 acquisition of PNA, as they historically turned their inventory at lower rates than Reliance.

Our outstanding debt at June 30, 2009 was \$1.27 billion, down from \$1.77 billion at December 31, 2008 and \$2.28 billion at September 30, 2008. Over the past nine months, we have paid down \$1.0 billion of debt with cash flow from operations and built our cash to about \$180 million. Our net debt-to-total capital ratio at June 30, 2009 was 30.7%⁽¹⁾, down from 41.4%⁽¹⁾ at December 31, 2008 and 48.1%⁽¹⁾ at September 30, 2008. In the 2009 first half, our capital expenditures were \$40.8 million, with much of this being growth related. Our initial 2009 capital expenditure budget of \$80 million has been increased to about \$95 million. We also continue to pay our regular quarterly dividend which is about \$7.3 million per quarter.

In May of 2009 we paid off the balance on our revolving credit facility. Our \$1.1 billion revolving credit facility and our \$500 million term loan expire in November of 2011. Beginning July 1, we have \$43.9 million of debt obligations coming due in 2009 and \$153.3 million in 2010. We are comfortable that we will have adequate cash flow and capacity on our revolving credit facility to fund these obligations. The covenants in our debt instruments primarily relate to maintaining a debt-to-capital ratio of less than 60% and an interest coverage ratio of at least 3 times. Our interest coverage ratio at June 30, 2009 was 5.2 times⁽²⁾. Thank you. We will now open the call for questions.

Thank you and we will now open the call for questions.

Regulation G Reconciliations

- (1) Net debt-to-total capital is calculated as total debt (net of cash) divided by Reliance shareholders' equity plus total debt (net of cash).
- (2) Interest coverage ratio is calculated as net income plus interest expense and provision for income taxes, less equity in earnings of unconsolidated subsidiaries, divided by interest expense for the latest-twelve months.

This conference call may contain forward-looking statements relating to future financial results. Actual results may differ materially as a result of factors over which Reliance has no control. These risk factors and additional information are included in the Company's Annual Report on Form 10-K for the year ended December 31, 2008 and other reports on file with the Securities and Exchange Commission.

QUESTION AND ANSWER

Operator

(Operator Instructions). Timna Tanners.

Timna Tanners - UBS - Analyst

UBS. I wanted to know if you could give us a little bit more detail on the outlook regarding demand and how much that might be customer restocking as you alluded to, and how much of that might be underlying demand improvement?

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

That is a very difficult question to answer. I think it is damn near impossible to answer. I think we are going to see some customers try to slide underneath these price increases. I think we are seeing that as we speak. On the other hand, the quoting activity that we are hearing from the field is very, very promising, and those are jobs that are up and coming and not like they are trying to slide underneath price increases.

So the answer to your question I cannot give you 100% guidance on that. Other than the fact that we are aware that some of our customers are going to try to slide underneath the price increases. But the quoting activity that we are seeing today is healthier than it has been in the first half of the year. And we think quite a bit of that is new jobs or maybe jobs that we were planning on starting at the beginning of the year. But because prices were sliding, they backed off, and now they are back in because they are seeing prices firm up.

Timna Tanners - UBS - Analyst

Okay. And then along those lines, is there anymore sensitivity to price increases than you have seen historically given the economy at the current time?

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

No. No, I think our customers realize that prices went down so dramatically that at some point in time they were bound to go up. So no, passing the price increases along. The only difference there is that it is still a very competitive environment. There is some destocking that is continuing to go on now, certainly not as much as it was in the first half of the year. But it is still competitive out there. But no, the customers they are not reacting negatively to the price increases.

Timna Tanners - UBS - Analyst

And then last question and I think along those same lines also, what would allow or might not allow your gross margins in the second half of the year to return to more normalized levels, maybe not the peak that we have seen, but for normal we have seen you at 26% to 27%. Can you just discuss the factors that may or may not allow you to get closer to that level?

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

Well, I think we would need some improvement in real demand in order to get that done. Certainly there are some things that will happen that will continue to improve our margins, and just a continued effort on getting some of the higher price inventory rolled out of our system. That, and coupled with replacing it with lower-cost material, is going to help our margins.

But the real catalyst, the thing that is really going to help and be meaningful is if real demand improves. And like we said, there are some spotty areas where that is happening. We think that there are some areas where it could happen some more, but we're not looking for anything to just take off. That just does not seem to be out there.

We don't see it getting much or any worse than what it has been. But, as we said earlier, every month this year demand has decreased on an average daily basis. So the smallest decrease of the year -- thank goodness -- was in June, and July seems okay. You know, for July, which normally tends to slow down quite a bit because of shutdowns and vacations, it has actually been -- a lot of our people are happy with what they have seen in the early half -- the first half of July. So that is encouraging to us also. But once again, we don't see demand just taking off at this point in time. But we also don't see it getting any worse, and right now that is a very good thing.

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Karla Lewis - Reliance Steel & Aluminum Co. - EVP & CFO

And I think, too, we talked about our inventory cost, and that definitely has a positive impact on our gross profit margin. So for certain of our products that are moving and that are turning well, we have seen a good improvement in our gross profit margin, maybe not back to our historical norm but getting much closer. And, as Dave was saying, as demand starts to improve across the board, that more of our C and D type items can start to turn and we can bring our costs down. That will all contribute to continuing to increase our gross profit margins.

Timna Tanners - UBS - Analyst

Great. Thanks very much.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

Hey, one other thing that we should probably tell you just so you can kind of put this in perspective. As you know from a LIFO standpoint, we estimate what our -- our method, which we have been consistent with because we have to, has been to estimate our LIFO adjustment for the year and then book 25% of it in each quarter. And each quarter we update that estimate. This last quarter we left it at \$300 million. That was the most reasonable estimate that we could come up with.

Just so you know our actual -- if June 30 was the end of the year, we would have booked \$243 million of LIFO income instead of the \$150 million that we have already booked.

Karla Lewis - Reliance Steel & Aluminum Co. - EVP & CFO

Yes, so our current estimates factor in the \$75 million per quarter continuing for the rest of the year.

Timna Tanners - UBS - Analyst

So we could see a reversal then of the LIFO income given that the trends are changing in terms of commodity costs?

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

No. We think that \$300 million is still a very good estimate as far as we are concerned right now. We just expect the rate of actual LIFO income if you will -- or the credit from LIFO to slow down in the second half of the year obviously. Otherwise, if it was equal, we would be looking at \$486 million of credit, and we started the year with less than that. So we could not have more reduction and reserve than we have reserves.

Karla Lewis - Reliance Steel & Aluminum Co. - EVP & CFO

Actually, I think Dave's main point he was trying to get across was that if we would be on a different method where we have booked our actual, which some other companies in our industry are, we would not have had a loss this quarter.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

Thank you.

Operator

Michelle Applebaum.

Michelle Applebaum - Steel Market Intelligence - Analyst

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I'm with Steel Market Intelligence. I'm just wondering I missed some of the beginning of the call. Did you address why you did not update your guidance in the quarter? I don't recall the Company having a miss before.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

Well, yes, that is because we really have not had many. We have had some misses, but we have missed -- mostly when we miss, we miss on the other side very honestly.

Michelle Applebaum - Steel Market Intelligence - Analyst

Yes, I remember a lot of beats, those are called beats, for the record.. I will send you a guidebook.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

Okay. Thank you.

Michelle Applebaum - Steel Market Intelligence - Analyst

You are welcome.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

By the time we really knew where the quarter was going to fall out, it was so close to today that we did not think it was meaningful to go ahead and update the guidance. If we would have at two months through the quarter, we had a sense that it was going to take some extraordinary things during the month of June for us to hit somewhere near the guidance. But we did not have a better estimate than that. There were too many moving pieces, and we could have come out and said, we are not going to meet the \$0.15 to \$0.20, but we don't know what we are going to do. And that did not seem to be very useful, so we did not do anything.

Karla Lewis - Reliance Steel & Aluminum Co. - EVP & CFO

Our business is very transactional, kind of day to day type business. It is very diverse touching very many different customer end markets, and we were hearing about some positive things into this pocket but some negative things in this pocket. Prices were going different ways for different products. We were seeing some GP improvement on certain items.

So the reason is the same it has been in other quarters when we have not updated, as Dave said. We have got some quarter-end adjustments like LIFO and receivables that we don't know, and they can be significant, and we don't know those until pretty close to the earnings stage.

Michelle Applebaum - Steel Market Intelligence - Analyst

Okay. I would normally read a non-update that had happened in June, but you knew you were not going to do the \$0.15 to \$0.20. So it was not just June. So where I was getting concerned and I think others might, is that you're guiding for a profit for the third quarter. And if this was all a June event, that would be a little bit more of a reach is what I'm saying.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

No, we feel pretty good about the fact that we will return to profitability in the third quarter. So we are much more comfortable with that than we were our guidance that we gave for the prior quarter.

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And one thing, Michelle, one of the reasons -- we really discussed long and hard here about whether or not we should give guidance for the second quarter at the end of the first quarter. The reason that we did very honestly was because the analyst estimates were out there at very high levels, unreasonable levels in our minds, and we thought the best way to reel them in was to give some kind of guidance, and we gave our best estimate at that time. And our miss, we go through the process of evaluating what happened during the quarter and how does it compare with what we thought would happen, and it was a revenue dollar issue driven by two things and two things only. One was the pounds or the volume that we sold was down 7% compared to the first quarter. We thought volume was going to be flat when we developed our guidance.

Karla Lewis - Reliance Steel & Aluminum Co. - EVP & CFO

And that was one of the things during the quarter we would see it was going down a little bit, but we kept thinking that May was going to get better, June was going to get better because the volume was down a point.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

And there were some signs at the end of the third quarter that certain prices had bottomed out.

Michelle Applebaum - Steel Market Intelligence - Analyst

Yes, I remember you saying that on the call.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

Yes. Carbon flat roll --

Michelle Applebaum - Steel Market Intelligence - Analyst

And then they bottomed again.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

Yes, they bottomed again. Some of them bottomed again and again. So instead of prices being down about 7.5%, which is what we had anticipated in our guidance, average pricing was actually down 14%.

Michelle Applebaum - Steel Market Intelligence - Analyst

It is all falling out very consistent. I think next time my suggestion would be I think you would do us all a favor to not give the specific guidance and perhaps just say the Street is too high if that is the only message you are saying.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

Yes, well, that is true, and that is good advice, and we will take that.

Michelle Applebaum - Steel Market Intelligence - Analyst

Well, I'm used to a very high degree of precision from Reliance Steel. Very low maintenance stock. Management always keeps you informed. Never -- I don't think you ever missed to the downside before in my almost 20 years covering your stock. So I think you are more than entitled one miss.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

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Well, thanks. We are not pleased with it, but it is what it is, and we are headed up from there.

Operator

Luke Folta.

Luke Folta - Longbow Research - Analyst

Longbow Research. My question for you guys this morning, just regarding the cost mismatch margin issue in the second quarter, are you able to quantify how much of an issue that -- you know what the impact was on gross margin as a result of that?

Karla Lewis - Reliance Steel & Aluminum Co. - EVP & CFO

Actually from a gross profit standpoint, the second quarter LIFO gross profit income came in a little bit better than we were anticipating. Most of it was just the fact that it was competitive replacement costs continuing to fall mainly for structurals and plate, and we still had some of the higher cost inventory in there. So we started to see that working itself out as mill pricing has stabilized, we believe, and started to go up.

So we don't -- LIFO income was 22.8% in the second quarter compared to 22.7% in the first quarter. Our FIFO gross profit was down from the first quarter and the second quarter, but quite honestly, based on the price increases, probably not as much as we had expected.

Luke Folta - Longbow Research - Analyst

Okay. I guess I was just trying to get a sense of what the drag was on the quarter that might not be there in the third quarter and the back half.

Karla Lewis - Reliance Steel & Aluminum Co. - EVP & CFO

Well, with the continued demand deterioration that we experienced and the fact that there were mill price decreases during the quarter.

Luke Folta - Longbow Research - Analyst

I mean are you able to give us some sort of feel on what the number there could have been from a dollar or margin basis?

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

No, we couldn't. But it would be nice if we could but we can't. We don't know how to come up with that kind of --

Karla Lewis - Reliance Steel & Aluminum Co. - EVP & CFO

I mean depending on what you are looking at but from what we were anticipating for the quarter, as Dave said, it was in the revenue line, not really in the margin.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

Yes, we expected the GP to be pretty much where it was, but we expected to have a fair bit more revenue dollars. And then when you apply that same GP percent, we would end up with more gross profit dollars and not the bottom line that actually occurred.

Luke Folta - Longbow Research - Analyst

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Okay. Thanks for the color there, guys. And just one more, regarding the overall mood of the M&A environment, we saw a lot of these smaller service centers with the financing environment not improving that much. I mean do you think the opportunities are going to start increasing for you to possibly make some acquisitions or possibly even see some of the smaller guys exit the business over the course of the back half of '09, 2010?

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

Whether it is the back half of '09 or starting in 2010, I think more likely it is going to be in 2010. Most of the service centers did pretty well from 2004 through 2008 really. The end of 2008 was painful, but the year was pretty good for most. So the balance sheets were in pretty good shape.

I do think though that the pressure on financing will really come to light when business does start to pick up in a material way. Because some of them folks may not have the financing they need to support their working capital increases for the new business levels, and that I think is going to spur some M&A opportunity. I don't know that that is going to happen in the back half of 2009. I don't think so. Maybe we will start to see some discussions, but I don't think you are going to see much by way of transactions.

There is virtually nothing out there now, certainly nothing attractive to us. And then you are going to have some business owners that are going to make it through this successfully, but they are going to say, we don't want to do this anymore. This was a real tough thing to go through. I don't want to risk my family's wealth by going through another thing like this. And there will be another one some day out in the future, hopefully not as bad as this. This is the worst thing we have all been through in our careers.

But there will be downturns again, and I think we saw that after 2001, 2002 and 2003 where some people took that attitude and said, you know, we just don't really want to take the chance of going through this again or leveraging up to do what we really need to do to build our business back to where it should be.

Luke Folta - Longbow Research - Analyst

Thanks again, guys, and congratulations on the balance sheet improvement and the cost efforts that you have been able to accomplish.

Operator

Mark Parr.

Mark Parr - KeyBanc Capital Markets - Analyst

KeyBanc Capital Markets. It was a tough quarter, a tough quarter for everybody. So I see there has been a little profit-taking today, but I think people are really focused on the fact that you guys are executing so well on the things you can control -- working capital, fixed costs, maintaining your pricing discipline in the marketplace. The end market is going to do what it is going to do. So for whatever it is worth, I just want to say you guys are doing a great job in a very difficult environment, and keep up the good work.

I had a couple of questions if I could. If you could -- and I don't ask questions like this very often, but could you give us an update on your sense of the inventory position at PNA, particularly related to beam inventories?

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

They have improved significantly since our acquisition of them on August 1 of last year. As a matter of fact, we are very proud of what they have done in most all of their -- the six companies that made up PNA. I'm not going to say we are proud of the profitability that we have had at PNA, but I am proud of the efforts that have been put forth in reduction of those inventories.

So unfortunately the odd part is -- you know, we talk about it and I dream about it all the time, is that we take \$1 billion out of our inventory, and our inventory turn does not go up. That is staggering to me. And it is kind of the case with them. They have taken a tremendous amount of dollars out of their inventory and tons out of their inventory, but because of the demand situation, their inventory turn really has not improved.

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Mark Parr - KeyBanc Capital Markets - Analyst

Okay. The turn has not improved, so that gives us kind of my follow-up question is, I think that their turns were probably below Reliance when the acquisition was made. So I guess what you're saying is that their turns are still below Reliance ex-PNA, but at least they are not losing ground. Is that kind of what you are saying?

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

Yes, it is. And, you know, let me tell you, when you get into the beam inventories -- even at Reliance companies that are in the beams and we are big in beams besides just with them -- beams always turn less than what Reliance's ordinary inventory turns are. That is just the nature of the beast. They can stock seven different lengths on one section of beam, and that just does not equate to good inventory turns.

Mark Parr - KeyBanc Capital Markets - Analyst

Yes, the supply pipeline is more disjointed because of rolling schedules.

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

Absolutely. No question about it. And then the section, I mean there is no other product that we have -- I should not say none -- but there are very few products that we have that you have to carry so many different lengths and so many, you know, one individual section. But they are improving, and their attitude is very well. They are very open to improving their turns and generating more cash flow, and we are proud of what they have done in that respect.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

The actual numbers are they were at the beginning of the year about 2.7 turns for the first quarter, and they are about 3.1 turns for the first half of the year. So they have improved to Gregg's point, and now our total Company turns -- and this is based upon dollars for the first half -- is 3.4. So they are below us, but they have improved also. And when you look at it in tons, it is better. So they have made a lot of progress on moving tons of material out.

You know, that was just -- it was just unfortunate that when we acquired PNA, which we are very glad that we did, we had about two months or three months of good business levels and then kind of everything hit the fan in November, primarily in the carbon plate and structural products. And we just did not have enough time to work through like we had with some other acquisitions, the best example being Jorgensen. That was kind of the opposite where we closed that deal April 1 of 2006 and things were humming and headed up, and we were fortunate in that regard. We were unfortunate here.

But we don't buy these things for what is going to happen in the next 12 months or the next six months or the next 18 months. So they are making progress. We are getting through it. We have got great management teams, and their attitude is good, as Gregg mentioned, and we are enthused, and we are looking forward to just working out from under this stuff.

Mark Parr - KeyBanc Capital Markets - Analyst

You know, Dave, just to be, in all honesty I think with the market willing to basically double your stock price since the beginning of the year, it is a tremendous testimony to your ability to handle the challenge that was presented to you by the unfortunate macro events around the PNA acquisition.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

Well, thank you. I could not have said it better myself.

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Mark Parr - KeyBanc Capital Markets - Analyst

So I mean, hey, look, the market is really the last word on all this. We could sit and talk about it all day long, but the market is saying you're doing a heck of a job.

So one other question I had, if you could just update us overall, could you give us some sense of your total -- for the total Company, a sense of what your automotive mix is, and what your commercial construction mix is, and then I will pass it on?

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

Automotive in terms of selling metal is virtually nothing. We do have exposure to automotive through our big coal processing operation, Precision Strip. And, by the way, they are -- they have no inventory, which is kind of a nice thing at this point. But they have done excellent job managing through this automotive turnaround. 60% of Precision Strip's business is automotive-related.

Now a good -- probably the majority of that is related to the transplant as opposed to Detroit. But nonetheless, the transplant business has turned out quite a bit as well. But they have done an outstanding job. They have maintained profitability, and we are very happy with that. So from an automotive standpoint in terms of selling metal, it is not --

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

It is basically zero.

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

As far as the structural side or the construction side, about a third of our business is non-residential construction related. And the commercial and industrial part of that is the difficult part. But there is -- you know, we include in that infrastructure and bridges and roadwork and those kind of things. And there has been some of that going on. Schools and hospitals have been pretty steady. So there are some bright spots in that in terms of -- not that it is increasing a lot, but it just has not fallen off like the commercial and industrial side.

Mark Parr - KeyBanc Capital Markets - Analyst

Okay. Terrific. Thanks for all the color. I really appreciate it.

Operator

Sal Tharani.

Sal Tharani - Goldman Sachs - Analyst

I just wanted to go back to destocking, restocking comments that have been made. Has there been any restocking at your service center or in general you are seeing, or is it more of end users who have run out of stocks and are ordering in to just bring them in line with the current demand?

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

I think it is a little of both. As we have reduced our inventories to the extent that we have, taking over \$1 billion out the last nine months, we are getting to the point now where, yes, we are restocking.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

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Especially those A and B items.

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

Yes. If you have anybody that can buy the C and D cell, let us know, we would like to sell some of those. But so yes, we are restocking. Our customers they have taken their inventories down just as far as we have, not knowing when the prices were going to hit bottom, and just I think a lot of it has to do with credit, too. The banks are on them, and they need to generate cash flow. So inventory reduction is a natural part of that.

So I think you're seeing it from both sides. I think service centers, ourselves included, are beginning to restock, as Dave pointed out, particularly the A and B items, and I think our customers' inventories have gone down to the point where they have to start replenishing.

Sal Tharani - Goldman Sachs - Analyst

Also, I just wanted to get a color on the size of the business. I mean you have a much larger business now than compared to three years ago, and granted it was the worst economic downturn we have ever seen. But has this been helpful? Because it is still a fragmented business and you have so many divisions, so many products. Has this helped you, or do you think it was better to manage a smaller business?

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

No, I think it is helpful.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

There is one thing and one thing only that has caused us to dip into this loss position, and that was very honestly the PNA transaction. And it was accretive for us last year. It has not been this year. Without -- and just so you know, we are not trying to throw water on anything -- but just so you know, without the PNA business in there, we would have been solidly profitable for the quarter. But we are not complaining.

As I said earlier, we don't do these transactions for a quarter or two or even 12 or 18 months. We do it for the long term, and we think there is good value in that business. But that is the single difference. We did not have them last time when we had the downturn, and we did not dip into any negative numbers. But it was because of that and it was because of some purchasing decisions, primarily made by people who are no longer with the Company, that have caused us to have really too much inventory at too high a price in some of those operations. But we are going to get through that.

Karla Lewis - Reliance Steel & Aluminum Co. - EVP & CFO

And in regards to the size, one of the things that has been helpful, and we talked a little bit more about it last quarter, was because of our size, we had a lot more outlets for our inventory when demand fell. If we would be a one or two location company, we could have only sold it to our customers. And because of our increased size and number of operations, we were at one location where a product was moving, instead of them purchasing from a mill, they got it from one of their sister Reliance companies. So that was, we think, something that we benefited from but many smaller companies did not have to help them through the difficult times.

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

One of the major problems that happened -- Dave alluded to it a minute ago -- that some of the people that got us into an inventory problem are no longer with the Company with the PNA Group. But there was quite a bit of metal that was being purchased going long speculating in offshore. Those practices have stopped, and they are not going to continue going forward. And I think if we would have had the opportunity of having PNA in our fold for 12 months prior to this downturn, it would have been a completely different scenario.

Sal Tharani - Goldman Sachs - Analyst

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Got it. You mentioned that there is still some destocking in some areas. Are there any particular products there where it is more so from the service center than the others?

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

Yes, plate. Plate probably -- not probably. Plate is definitely the worst. And there again, it is a perfect example of people going offshore buying a lot of plate and the plate coming in at extremely inflated levels, and the orders were placed. And I'm not talking about just Reliance, okay, or PNA; I'm talking about the market place in general. And a lot of this product was placed offshore based in the July, August, September timeframe at exorbitant prices at the height of the market based on usage of the first half of last year, which, of course, did not come about.

So there is a lot of this high-priced plate that has been in the marketplace since the beginning of the year, and it is being flushed out. But there was a lot of it. I mean not a little of it. There were a lot of tons of plate, and they are still out there. If we have a problem -- if we are destocking any item today, it is plate. Basically the rest of our product line for the most part is a pretty good line.

Sal Tharani - Goldman Sachs - Analyst

Okay. Last, if I heard correctly, you have raised your CapEx for the year by about \$15 million. Can you give us some color on that, please?

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

Yes, it was really a couple of things. There are a couple of pieces of property that we leased in one of our subsidiaries that there are purchase options on those pieces of property, and it is a window kind of midway through the lease, and it makes a lot of sense for us to financially to go ahead and buy those properties. So that is why we increased it.

Karla Lewis - Reliance Steel & Aluminum Co. - EVP & CFO

It will be a net improvement for our expense line.

Sal Tharani - Goldman Sachs - Analyst

Great. Thank you very much.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

If it does happen this year, it will happen late in the year. It could also slop over into the earlier part of next year.

Operator

Tim Hayes.

Tim Hayes - Davenport & Co. - Analyst

Davenport & Co. Just a couple of numbers questions that I missed. In terms of carbon steel as a percent of revenue during the quarter, was that 57%?

Karla Lewis - Reliance Steel & Aluminum Co. - EVP & CFO

Correct.

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Tim Hayes - Davenport & Co. - Analyst

Okay. And then what was the sequential change for average selling prices on a same-store sales basis?

Karla Lewis - Reliance Steel & Aluminum Co. - EVP & CFO

That was --

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

For the quarter or for the half?

Tim Hayes - Davenport & Co. - Analyst

For the quarter, Q2 versus Q1.

Karla Lewis - Reliance Steel & Aluminum Co. - EVP & CFO

Average selling price was down 12.4% Q2 from Q1.

Tim Hayes - Davenport & Co. - Analyst

Okay. That's all my questions. Thanks.

Operator

John Tumazos.

John Tumazos - Indie Research, LLC - Analyst

Independent Research. Congratulations. I wish over 15 years I just had one misstep. Now it seems like all the nonferrous prices are rising due to both global and US improvements, and just to take the container board industry as an example, in three months the operating rate has gone from 77% to 91%. Steel is lagging, but it is up, too.

You are a little cautious today where it would seem like both the ferrous and the nonferrous prices are going up with scrap quotes up 140 to 180 a ton from their lows. Are you seeing continued declining consumption in aerospace, oil field, heavy construction, such that use the adverse volume variances or maybe some high cost inventory you have still got to get out the door in the third quarter? Or are you concerned about an economic double-dip because so many of the heavy markets are not moving ahead very quickly?

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

No, I think it is the former, John. We are concerned about that. We are not really thinking about a double-dip, don't want to think about a double-dip. But no, we have the oil business. As I mentioned when I went through it kind of by product, the largest percentage decrease in tons sold in any of our products last quarter was in the alloy side, which is primarily the energy oil and gas related product. And that was down 26%. So no, we don't see that falling a lot further. I think if we are not at the bottom there, we are darn close to it. But we don't have a lot of confidence that that is going to take off.

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

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Commercial aerospace, as you know, is in regional jetliners and business jets and whatnot. That has been slow for the first half, certainly in the second quarter. We don't expect any improvement there at all.

We have done well on the military and defense side of the business. There's indications that that because we actually have backlogs in that product mix and that industry, and we look for a slight decline in that going into the second half of the year. But, as Dave pointed out I think in his opening remarks that is one of our most profitable businesses. So a modest decline, that is alright to us.

But energy, we do expect that has slowed. No question about it, but it is still our second best performer.

John Tumazos - Indie Research, LLC - Analyst

I don't want to maybe get too specific, but it seemed like the corporate culture from when I first met you in 1994 was to buy inventory to sell in that current period and not speculate. And the acquisitions that some people get, I guess, too excited in the boom times in '07 and '08. Could you just give us a little color on how you are controlling things to make sure that the purchase orders are not excessive going forward?

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

That culture has not changed, John. That focus on inventory control and inventory turn is still here in spades. But some of the companies, not just PNA, but some of the other companies that we have acquired over the years have not had that focus. I would say every company but maybe one has turned their inventory 10 or 12 times when we acquired them and is still doing so. But every other company we have acquired we have worked with them to improve their inventory turns.

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

We have not had a company ever that we have acquired -- and I think we have acquired over 45 since our IPO -- that has not improved their inventory turn. The difference is is that the mix, you have got to look at the mix. Beams, which as a percent of our carbon steel or even our total, is the largest, and plate is right next to it.

Both of those are about identical. Karla? 13% each. So that is a huge part. Both those commodities do not turn as well as flat-roll. And flat-roll when we first went public was a much greater percentage of our sales than it is today. We think that is a good thing. But it is going to have an impact on your inventory turn bringing it down. But as far as our emphasis on inventory turn, you can feel free to give anybody in our Company a telephone call and ask them if they don't hear about inventory turn until they are sick of it.

Karla Lewis - Reliance Steel & Aluminum Co. - EVP & CFO

From an acquisition standpoint, that has not changed. We knew that PNA did some speculation. We knew there were some orders out there, the same as there have been with many of our other companies when we have bought them over the years, and we have tried to quickly explain to them we don't do that. I think the difference -- two things that happened here was one, PNA is the largest company we have ever bought. So the quantity, the volume of inventory that they had on speculation when they bought them was bigger. And two, the market just fell out from under us in a way that had not happened on some of our prior acquisitions where they had some tons out there long.

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

Right. And when you have that product, John, as you know, on order offshore through trading companies, when it is on order, it is on order. It is going to come in whether you like it or not, and we are certainly not going to go back on their words. So we accepted that material reluctantly, but nonetheless we did accept it. But it will turn around.

Karla Lewis - Reliance Steel & Aluminum Co. - EVP & CFO

And there have been controls put in place. I think everyone at PNA is very clear on how we feel about it, and they need to take any foreign buys through Gregg now.

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Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

Yes, there are no foreign purchases made without approval of our office.

Operator

Dan Whalen.

Tony Rizzuto - Dahlman Rose & Co. - Analyst

You know what, this is Tony Rizzuto. You may be referring to me perhaps from Dahlman Rose. Listen, I have got several questions here. First of all, when you made the comments on plate, can you update us on where the carbon plate typically go to? Because I have been hearing that the demand for wind towers has really hit a wall. What are some of the other major areas of offtake? And I have got a couple more follow-on questions as well.

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

Well, you know wind tower is good. Well, it is not good. I mean it is a good portion of it, but we do railcar and that is off. Okay, that is definitely off. But the bridge, a lot of it goes into that. It goes into -- you know, when they are building arenas and stadiums and whatnot, a lot of that goes in there as far as --

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

Barge work.

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

Yes, barges. That is big.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

That is a big customer for us. A big industry for us.

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

And it is actually doing quite well.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

That is doing alright.

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

And just typical most the infrastructure in nonresidential construction, all of those areas are plate is big in.

Tony Rizzuto - Dahlman Rose & Co. - Analyst

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All right. And when you were talking about schools and hospitals as doing well, could you guys narrow that down in terms of what percentage of your nonresidential activity would you say are projects which have been underway and may be previously financed versus kind of new business, if you will?

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

That is really hard for us to do because we are selling not the projects direct most of the time, we are selling fabricators, and it is just very difficult for us.

I will say that from what our guys tell us that the commercial and industrial area is more where projects are a kind of finishing and there are not as many new projects out there. But on the schools and municipal kind of things, hospitals, those things tend to be more steady. But in terms of how much of that third is one or the other, we just don't know.

Tony Rizzuto - Dahlman Rose & Co. - Analyst

Alright. And I have just got one more question, and I know -- I think Gregg you made earlier comments about the alloy heat treat plate market and you indicated that it was clearly softer. And I'm just wondering with all the problems, the continuing problems that Boeing is having -- and I know you guys, your forte is really military and defense. But I oftentimes have seen the big mills participating in the aerospace heat treat. They come down into the 60, 61 market. I'm just wondering do we have a flooded situation out there in terms of inventory in the pipeline? Are you seeing the mill suppliers cutting back from a utilization standpoint?

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

No. You know, I would like to think -- and I'm not 100% on this, Tony -- I have to tell you that, okay? But is there an abundance of supply? The answer is yes. Okay? Have prices come down? Yes. Has it run into commercial grade 60, 61? Has 2 and 7 series affected that? Yes. So just aluminum plate in general whether it is aerospace-related, commercial 61 related, okay, there is a lot of plate out there that is readily available.

Tony Rizzuto - Dahlman Rose & Co. - Analyst

You guys have been around. You have seen these cycles. How do you compare what we are in right now from that side alloy heat treat to what we have been and what we have been through the severity right now versus other cycles you have seen?

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

I think we have seen cycles similar to this. Boeing is historically -- their build rates and their forecasts and what their expectations are and all that has always been a little bit unreasonable. And their inventories I mean one of the things that is hurting I think the industry as a whole there was take and pay agreements that Boeing entered into with the major suppliers, and they are taking it and they are paying it.

So their inventories are building, which has a negative impact on those people that are going to supply commercial aerospace and service centers in the future. Fortunately for us, our involvement on the commercial side of Boeing's business is not that great, but it affects everything else. We are big on electronic semiconductor equipment, which is a big, huge 60, 61 market. It slops down into there. It negatively impacts the pricing, okay, and that impacts our business in areas other than commercial aerospace. But there is a whole lot of aluminum plate out there, Tony.

Tony Rizzuto - Dahlman Rose & Co. - Analyst

Gregg, is this something that has accelerated, or has this been underway, and we are kind of stabilizing or kind of coming to the bottom of this thing? What do you think? What is your best guess right now?

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

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That is a hard question to ask. I guess my emotions want to say that it is stabilizing. My business sense is that as long as that dreamliner keeps getting postponed, postponed, postponed, postponed -- okay -- that is a problem. And it is not only with aluminum plate; it is titanium; it is the whole nine yards. And there is just not -- I don't know it just seems to me like supply is much greater than demand, and I don't know how far that they can take down production levels.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

That has been going on, as you know, Tony, for quite a while. The 787 has been pushed back a number of times, and A380 also has at Airbus -- has an impact on that. Whereas it is better now than it was, but I don't think they are building at the rate that they had hoped to be building at now. So all of those kind of slowdowns have just kind of backed material up in the market, and the more they get pushed back, particularly in light of these take-or-pays, that is just creating a little more metal as we go in the marketplace.

So it has been going on for awhile, but like Gregg said, we would like to think that it is stabilizing, but it is just building up steadily. And, you know, we were talking just yesterday that we were actually a little surprised that the prices have not come down more than they have.

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

Yes, especially on the 2 and 7. But the good news is, Tony, on the 60, 61 side, we are seeing some increased activity on the semiconductor equipment manufacturing business, which is our largest segment of 61 sales.

Tony Rizzuto - Dahlman Rose & Co. - Analyst

That is Valex. That is Valex for you guys, right?

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

No. They are more into the stainless tubing, but the 61 is in a lot of our other companies -- Yarde, Bralco, Metalcenters.. But the build-to-book ratio is starting to trend up, which is something that we watch. And so it is people like Applied Materials, LAM Research, Novelis, those type companies that support those sales, and we're getting some positive feedback. We are actually -- it is being backed up. We are getting orders.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

Some of that is related to the semiconductor and also the solar and the flat-panel LCD type industries. So those are looking more positive in the second half of the year.

Tony Rizzuto - Dahlman Rose & Co. - Analyst

Yes, but you know, I'm seeing the Chinese ramp up in some of these areas, too. And I'm concerned that maybe they can -- they are starting to supply perhaps some of that material as well. Are you seeing any of that?

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

Well, we sell some of that metal over there, Tony. I think the problem is the quality of the material made over there is not really sufficient for those, and they need our quality to feed into those applications.

Gregg Mollins - Reliance Steel & Aluminum Co. - President & COO

The problem with those applications, Tony, they are vacuum chambers. And if you have any porosity problems, it is going to cost you a tremendous amount of money. So quality is huge.

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Tony Rizzuto - Dahlman Rose & Co. - Analyst

Great insights. And I did not hear anybody ask the question, but with all the stuff going on with this new administration, has it changed your view of the -- are there any programs that run a risk of coming off here that have been important from a military or defense perspective for you in the balance of this year or 2010?

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

There are a lot of question marks out there, and so we will see how it all falls out. Just by way of example, I know the C-17 has been on the cutting line, not just in this administration but for a number of administrations, and it always seems to kind of survive.

So we will see if there are some things targeted like the F-22, but that might survive, too. And then you have also the opportunity which has happened in different programs that other countries come in and place orders for those things. So we will see. There are some question marks out there. There are a lot of question marks, by the way, with this new administration and the impact on business.

Tony Rizzuto - Dahlman Rose & Co. - Analyst

Well, you have been very gracious with your time. I appreciate all your insights as always, guys.

Operator

We have no further questions in the queue at this time.

David Hannah - Reliance Steel & Aluminum Co. - Chairman & CEO

Okay. Well, thank you all for listening. We are smiling here, believe it or not. It is better than it has been. For the first six months of the year, we see things finally trending in the right direction in terms of pricing, which is a huge factor for us. We have positioned the Company well, and we are excited to take on the challenges of the second half.

So thank you very much.

Operator

Thank you, ladies and gentlemen. This does conclude today's conference call. You may disconnect your phone lines at this time, and have a wonderful day. Thank you for your participation.

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