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Conference Call Transcript

RS - Q2 2010 Reliance Steel & Aluminum Co. Earnings Conference Call

Event Date/Time: Jul 22, 2010 / 03:00PM GMT

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PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the 2010 second-quarter financial results conference call and webcast. (Operator Instructions). It is now my pleasure to turn the floor over to your host, David Hannah. 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, 2010. 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 in the Investor Information section.

For the 2010 second quarter, Reliance reported net income of $61.6 million, or $.83 per diluted share, compared to the 2009 second quarter net loss of $5.8 million. Sales for the 2010 second quarter were $1.62 billion, up 30% from the 2009 second quarter sales of $1.24 billion, and up 11% from 2010 first quarter sales of $1.45 billion.

Additionally, the 2010 second quarter net income and earnings per share were up 38% compared to the 2010 first quarter on an 11% increase in sales, resulting from improved shipments and pricing during the quarter combined with only a 1% increase in operating expenses.

For the six months ended June 30, 2010, net income amounted to $106.2 million compared with net income of $14.3 million for the same period in 2009. Earnings per diluted share were $1.43 for the six months ended June 30, 2010 compared with earnings of $.19 per diluted share for the six months ended June 30, 2009. Sales for the 2010 year-to-date period were $3.07 billion compared with 2009 six month sales of $2.8 billion. Karla will talk more about the LIFO adjustments and how they impact the comparisons of the 2010 and 2009 periods.

We sold 951,000 tons of metal during the 2010 second quarter, up 9% from the 2009 second quarter and up 4% from the 2010 first quarter. Average prices per ton sold in the 2010 second quarter were up 19% compared to the 2009 second quarter and up 8% compared to the 2010 first quarter. For the 2010 second quarter, carbon steel products were 52% of net sales; aluminum sales were 18%; stainless steel sales were 15%; alloy sales were 8%; toll processing revenues were 3%, and other sales were 4%.

By product, compared to the 2010 first quarter, carbon steel sales of 784,000 tons were up 3% with average pricing up 9%; aluminum tons sold of 56,000 were up 6% with pricing up 2%; stainless steel sales of 47,000 tons were up 4% with prices up 11%, and alloy tons sold of 46,000 were up 7% with pricing up 4%.

Generally, the quarter just ended was slightly better than we expected as volumes sold and pricing for all products improved a little more than we earlier anticipated. Gross profit margins(1) on a FIFO basis were also fairly steady through the quarter. Our sales per day increased in April and May by 1.4% and 6.7%, respectively, and decreased 1.6% in June as prices softened some, which has an impact on our customers' buying patterns.

Overall, we were very pleased with the quarter's results. Our balance sheet continues to be strong. Receivables and inventories are in good shape, we generated cash from operations of $19 million during the quarter, and ended the quarter with net debt-to-total capital of only 26%, down slightly from the end of the prior quarter.

Prices have recently softened some for most all of our products and we expect there may be some further decreases during the third quarter, but not to an extent where we are overly concerned. Also, demand looks to remain fairly steady at current levels and we do not expect any significant changes in either direction, except for some normal seasonal slowing earlier in the quarter. Given these expectations, at this time, we estimate earnings per diluted share in a range of $.65 to $.75 for the 2010 third quarter.

On July 21, 2010, the Board of Directors declared a regular quarterly cash dividend of $.10 per share of common stock. The dividend is payable on September 13, 2010 to shareholders of record August 20, 2010. The Company has paid regular quarterly dividends for 51 consecutive years.

Hopefully, we will now begin to recover some of the value that we have lost over the last 90 days, given the solid quarter just reported and since our outlook for the back half of this year has not really changed. In fact, our outlook for many of our markets is better now than three months ago (e.g. aerospace, semiconductor, electronics, and energy) and none of our markets look worse, even non-residential construction. We do expect a little seasonal summer slowness, and prices have certainly softened, but that is OK. I also believe we should see some attractive acquisition opportunities as the year progresses.

We have been saying for the last seven months now that overall, business is a little bit better and we expect slow and steady improvement. There will be some backwards or sideways steps in pricing and demand along the way, but that should not be a surprise to anyone. I do not believe that any broad based, real and significant economic improvement will occur until confidence in our country's economy and leadership at all levels is restored, and that will not happen until we put people back to work.

As I said last quarter, we are not worried about our performance. We will continue to grow and expect to perform at the top of our industry. Our company has tremendous earnings capacity and, with our broad product base and wide geographic footprint, we remain excited about our competitive position in the industry. Thank you. I will now turn the call over to Gregg for some additional comments on our operations and market conditions.

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

Thank you, Dave and Good Morning. As Dave pointed out we are pleased with our results in the second quarter. As expected, we saw a gradual improvement in demand throughout the quarter in most all the industries we support. In spite of a 9% increase in tons sold in the second quarter of 2010 versus the second quarter of 2009, our employee count has only risen 1.2% on a same store basis. We are very mindful of the deep cuts we made in our operations in 2009 and are very hesitant to add to our payroll. As always we continue to focus on improving our inventory turn. Our first-half turn, in dollars, was 4.8 times or 2.5 months on hand. In tons, we turned our inventory 5.1 times in the first-half and continue to make progress in many of our operations. We still feel there is room for improvement.

As all of you know, gross profit margins get a lot of attention at Reliance. Once again our sales people in the field were successful in passing through our higher cost inventory to our customers resulting in FIFO gross profit margins of 26.3% in the quarter. This was by no means an easy accomplishment given relatively weak demand and the competitiveness in the marketplace. When price increases are not demand driven customers shop around more and it is much more difficult to increase margins. Our hats are off to our people in the field that were able to make this happen. From a demand standpoint we have seen some small but steady improvements and believe this will likely continue into the future. We do expect to see the normal seasonal summer slowdown but nothing dramatic.

Agricultural equipment, infrastructure rebuild, bridge construction, barge manufacturing and tank building are all doing reasonably well. Electronics and semiconductor equipment manufacturers are doing quite well as is aerospace. Industrial construction such as power, transmission towers and alternative fuel projects are improving as we speak. Non-residential construction continues to lag but we feel as though we are at or near the bottom of the cycle.

As for pricing, carbon steel prices over the past few months have softened in all products but are still at higher price levels compared to the first of the year. This was no big surprise as the dollar strengthened and imports increased during the second quarter. We believe the domestic suppliers have done a good job managing the pricing side and exercising discipline. Lead times on most products are relatively short. We do not expect any significant discounts, like the ones we experienced in 2009, and feel confident we can manage our way through whatever conditions exist.

Midwest spot aluminum ingot is near $.95 a pound down from a peak of $1.17 a pound in April. On the aerospace side, there is still an inventory “over hang” on heat treat plate but with any luck this will correct itself by year-end. As I mentioned earlier, aerospace at Reliance is still doing well. As for stainless, the base price for stainless has remained flat so far this year. Nickel surcharges, on the other hand, have continued to be volatile. Nickel average monthly surcharges in June peaked at $1.27 a pound and have dropped $.31 to $.96 a pound for August delivery. Roughly half of our stainless sales are in sheet and plate and the balance is in bar and tube.
The significance of this is bar and tube are more profitable due to much smaller order sizes.

To conclude, we are confident in our ability to manage through any and all markets. Our management team throughout the Company is better, stronger and is more experienced today than ever before. Our operating expenses are as lean as they have ever been and we continue to manage our working capital well. We do not expect any real surprises, good or bad, and we intend to stay focused on making money and growing the business. I will now turn the program over to Karla to review the financials.

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

As Dave stated, we have continued to see steady, although moderate, improvement in our tons sold through the 2010 second quarter, with our highest monthly tons shipped per day since January 2009 and our highest quarterly sales dollars per day since 2008.
For the 2010 first half, our tons sold were up 3.1% and our average selling price was up 5.8%. Our average selling price improved due to the mill price increases, but also increased somewhat due to a shift in our product mix, with carbon steel representing 52% of our 2010 first half sales, compared to 57% in the 2009 first half.

Our 2010 second quarter gross profit margin was 25.7%, compared to 22.8% in the 2009 second quarter and 26.0% in the 2010 first quarter. For the 2010 first half, our gross profit margin was 25.9%, up from 22.7% in the 2009 first half.

Our LIFO adjustment was a debit, or expense, of $10.0 million in the 2010 second quarter, compared to a LIFO credit, or income, of $75.0 million in the 2009 second quarter and LIFO expense of $5.0 million in the 2010 first quarter. Our 2010 first half LIFO expense was $15 million, compared to 2009 first half LIFO income of $150 million. Our LIFO adjustment is included in cost of sales and, in effect, reflects cost of sales at current replacement costs.

We currently estimate our 2010 full year LIFO adjustment at $30 million, up from our estimate of $20 million at the end of the 2010 first quarter. Through the first half, our actual LIFO calculation results in LIFO expense of $36 million. Our estimate anticipates further reductions in prices and inventory quantities from current levels for many of our products through the end of the year.

Our FIFO gross profit margin for the 2010 second quarter remained consistent with the preceding quarter at 26.3%. During the first half we expanded our FIFO margins as mill prices increased and saw some pressure near the end of the second quarter as prices started to decline.
As a percentage of sales, our 2010 second quarter SG&A expenses were 16.8%, compared to 19.9% in the 2009 second quarter and 18.5% in the 2010 first quarter. The improvement is due to improved volume and pricing on a relatively consistent cost structure, with the exception of higher commission and incentive expense in 2010 as compared to 2009 because of our significantly improved profit levels.

Operating income for the 2010 first half was $194.4 million, or 6.3% of sales, significantly improved from $53.4 million, or 1.9% of sales in the 2009 first half. The improvement was mainly due to our improved gross profit margins and improved volume.

Interest expense for the 2010 first half was $30.7 million, down 14.7% from $36.0 million in the 2009 first half mainly because of our lower debt levels resulting from the record cash flow we generated throughout 2009 as well as improved working capital management.

Our other expense for the 2010 first half was $1.1 million compared to other income of $3.8 million for the 2009 first half. The change was mainly due to the timing of insurance proceeds and investment returns on our life insurance assets.

Our 2010 first half effective income tax rate is 33.7%, compared to our 2009 annual effective rate of 23.7%. In the first quarter, we estimated an annual rate of 31.6%. The increased annual rate resulted in a 2010 second quarter rate of 35.1%. The fluctuations in our effective tax rate are mainly because of our varying income levels over these periods.

Our net income of $61.6 million and our earnings per diluted share of $.83 in the 2010 second quarter are up 38% from our 2010 first quarter results.

Because of improved business conditions in the 2010 first half, we increased our working capital, using cash from operations of $35.5 million. However, we actually provided cash from operations of $18.8 million in the 2010 second quarter due to the diligent efforts of our management teams in managing their working capital. In the 2009 first half we were aggressively reducing our working capital, resulting in cash from operations of $681.3 million.

Our June 30th accounts receivable balance increased $202.9 million, or 38.0%, from the 2009 year-end because of increased sales. Our accounts receivable days sales outstanding rate improved to about 41-1/2 days at June 30, 2010, two full days better than 43-1/2 days at June 30, 2009. In general, the quality of our receivables has improved in 2010 over 2009.

Our FIFO inventory levels increased $192.4 million and our accounts payable and accrued expenses increased $123.7 million at June 30, 2010 from the end of 2009. The increased inventory levels support our increased shipments and we significantly improved our inventory turn rate to 4.8 times for the 2010 first half compared to 3.4 times for the 2009 first half and 3.7 times for the 2009 year.

We spent $39.4 million for capital expenditures in the 2010 first half, with the majority used to purchase two of our existing warehouses that we previously leased and to complete our EMJ facility in Malaysia that is now operating. Our 2010 capital expenditure budget is $140 million and includes many growth projects.

Our outstanding debt at June 30, 2010 was $1.0 billion, with borrowings of $189 million on our $1.1 billion credit facility. Our net debt-to-total capital ratio at June 30, 2010 was 26.1%(2), up slightly from 25.6%(2) at December 31, 2009 and down from 30.7%(2) at June 30, 2009. The covenants in our amended credit facility reset to our pre-amendment levels effective June 30, 2010 and require us to maintain 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, 2010 was 6.4 times(3).

We have about $150 million of debt obligations coming due before our credit facility expires in November 2010. As of June 30 of 2010 the restrictions in our credit facility on uses of cash, including funds used for acquisitions, dividends and investments, were also reset to pre-amendment levels.

We are comfortable that we have adequate cash flow and capacity in our revolving credit facility to fund our debt obligations, as well as our working capital, capital expenditure growth, and other needs in the near future.

I apologize. I said we had $150 million of debt obligations coming due before our credit facility expired in November of 2010. It is actually November of 2012. I apologize for that. Now we will open the discussion for questions. Thank you.

Regulation G Reconciliations

(1) Gross profit, calculated as Net sales less Cost of sales, and Gross profit margin, calculated as Gross profit divided by Net sales, are non-GAAP financial measures as they exclude depreciation and amortization expense associated with the corresponding sales. The majority of our orders are basic distribution with no processing services performed. For the remainder of our sales orders, we perform "first-stage" processing which is generally not labor intensive as we are simply cutting the metal to size. Because of this, the amount of related labor and overhead, including depreciation and amortization, are not significant and are excluded from our Cost of sales. Therefore, our Cost of sales is primarily comprised of the cost of the material we sell. We use Gross profit and Gross profit margin as shown above as measures of operating performance. Gross profit and Gross profit margin are important operating and financial measures, as fluctuations in our Gross profit margin can have a significant impact on our earnings. Gross profit and Gross profit margin, as presented, are not necessarily comparable with similarly titled measures for other companies.

(2) Net debt-to-total capital is calculated as total debt (net of cash) divided by Reliance shareholders' equity plus total debt (net of cash).

(3) Interest coverage ratio is calculated as net income plus interest expense and provision for income taxes, plus or minus non-recurring loss or gain, 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, 2009, the Quarterly Report on Form 10-Q for the quarter ended March 31, 2010, and other reports on file with the Securities and Exchange Commission.

QUESTION AND ANSWER

Operator

(Operator Instructions). Michelle Applebaum, Michelle Appelbaum Research.

Michelle Applebaum - ***Michelle Appelbaum Research - Analyst***

Nice quarter and nice guidance. It was a lot better than I expected, on both. So good job. Can I get a little bit more clarity on what you think the revenue trends and margin trends would be in the third quarter? I love the bottom line, but I would like to know how you get there.

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

Sure. In general, we expect July -- that is usually the time that we see the softness in the third quarter is primarily in July, and then it starts to get a little bit better through August. And then September usually ends up being the strongest month of the quarter. Do you have anything more that you can add?

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

Generally we assume that on a ton basis we expect the normal seasonal slowness that -- like Dave talked about in July, but we expect that to be offset a little bit by continued, steady improvement in a lot of our markets.

So tons are flattish to down slightly, and you also -- with pricing with the current trends, which hopefully will be offset a little bit later in the quarter a couple of percentage points down on pricing, that environment would put a little bit of pressure on the gross profit margin. So we take that down a little bit.

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

We are seeing the pressure on the margin in the first few weeks -- the first, what, how many business days we have had so far in July. But, again, it is reacting really like the whole second-quarter did, pretty much as we expected. We didn't really see any big surprises come up during the second-quarter. And at least so far in the third quarter, we haven't seen anything that is terribly unusual.

We always see tonnage per day go down a little bit when prices level out or start to go down, because customers will just wait to buy only what they need. That has been, I think, the trend for quite some time, Gregg. The customers have been very cautious, and just buying what they need for a couple of years, at least now.

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

Exactly. They got stung pretty bad back in '09, as all of us did, and they haven't forgot that trend at all, which is -- in the long run it has been to our benefit, because next day delivery is all the more important, and that is our model.

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

Yes.

Michelle Applebaum - ***Michelle Appelbaum Research - Analyst***

That makes sense. Can you comment, do you think that we are close to the bottom here in terms of the weakness in the market?

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

The one market that is still very weak is the one that everyone talks about -- the mills talked about it and we talked about it -- and that is the non-res construction market. We throw a lot of things into our non-res kind of group when we talk about it. Infrastructure gets thrown in there, and a lot of the things Gregg mentioned earlier in terms of construction of barges and bridges and water work projects and those kinds of things, public works projects.

Some of that stuff is actually okay, but the private commercial and industrial investment levels of construction, non-res construction, are the areas where it is still weak. It is still very, very weak, and we wouldn't even say that it has gotten any better, but the decrease or the weakness seems to have leveled out, or at least we are close to the bottom.

So our view today compared to our view three months ago on the non-res side is that our view is not any worse today than it was then. And we think we are closer to the bottom, if we are not already at the bottom. So that is a positive view, I guess, if you want to put it in that perspective.

Michelle Applebaum - ***Michelle Appelbaum Research - Analyst***

Then one more. You sounded more optimistic on acquisitions. Did I read that right?

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

Yes, you picked up on that, huh?

Michelle Applebaum - ***Michelle Appelbaum Research - Analyst***

A little slow.

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

I think that, again, what we have been saying is that we thought as the year progressed we would start to see some opportunities that were attractive to us. And the year is progressing and there are some things out there that we would say -- or if they are not out there yet, we would expect over the next six months. As we said before, the back half of this year we would expect to start seeing some change in the mindset of some of the business owners.

I think there is some consideration for the anticipated increase in tax rates the first of the year. I think that is -- at least some of the discussions that we have been having with people, it has been evident that some of the business owners are thinking about that, because if they wait they may be able to sell their business for a little bit more, but they may net a little bit less because of the increase in tax rates.

So people are thinking about that. And I think, as we thought earlier in the year, that is going to pick up and we should start to see some opportunities.

Operator

Timna Tanners, UBS.

Timna Tanners - ***UBS - Analyst***

Just a few questions. So I wanted to dig down a little bit more also on the demand side and hear your views of what your customers are telling you what their credit availability are and how that has trended recently.

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

As far as their --?

Timna Tanners - ***UBS - Analyst***

Access to credit for your customers.

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

We really haven't seen any problem with that. Karla, can you comment on that?

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

We haven't seen a major trend, because we believe that because things have remained fairly steady, although there certainly is some volatility going on in pricing and demand, we think that our customer base can for the most part maintain throughout that, and unless they have a line coming due, won't need to approach their banks.

What we have said for a few quarters now is we think that there would be a significant upturn where they would have to rapidly ramp up their working capital, and pull on those lines, then we might see some issues.

But it is -- we have continued to see some write-off activities, probably a little more of that has been in the non-res area, because people have worked through their cash and are running out, but nothing significant -- and there is a customer here and there, but overall they are maintaining fairly well right now.

Timna Tanners - ***UBS - Analyst***

Okay, great. Thanks. I wanted to understand stainless a little bit better, because I think I probably got carried away getting concerned about it maybe. But it just seems to me like a lot of customers were getting out of the market until they got some visibility on nickel solidifying.

I know you guys always were uncomfortable with some of the volatility there. But what trend have you seen in orders there from the recent months, and what are you expecting going forward, and how might that impact your segments?

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

This is on the stainless?

Timna Tanners - ***UBS - Analyst***

On stainless, yes.

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

I think before -- when I gave the by product information there, you probably saw that the average pricing on stainless was up more than pricing on any other of our product groups during the quarter. Average pricing on our stainless sales was up 11% and tons were up 4%. That was really driven by what Gregg is going to talk about now, which is the increase in the nickel surcharges through -- pretty much through the entire first-half. It pretty much stepped up month by month, didn't it, Gregg?

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

It sure did, and fairly significantly. It started out -- a nickel surcharge in January was about $0.70 a pound. It peaked at $1.27 in June, which is obviously a significant increase. There was some hedging going on by our customers, as expected. Because our salespeople and our customers are well aware of the increase and the charges going forward, so people that are buying stainless were definitely going on and trying to get underneath some of those price increases, which is why you're asking the question, what are they doing now when surcharges are going down. They're holding off.

So we expect that our stainless sales, until we bought them out on the surcharge will deteriorate somewhat. But there is still a need for demand. So they're going to have to keep replenishing, but they're not going to be hedging, that's for sure.

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

They will buy only what they need to do whatever is in their--.

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

-- project they have got.

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

Because the one thing with stainless that I know that drives the mills nuts, but it also drives us nuts, is that visibility a month in advance or more on what the surcharge level is going to be. So that is why you hear and you read about certain people from the mill perspective selling today at anticipated discount or anticipated surcharge levels in August or September.

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

So when you apply that to looking at Reliance, stainless is a very important part of our business, but if you're trying to factor it in, remember stainless is 15% of our total sales dollars. And with the hedging we went up 4% in the second-quarter so --.

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

Right. There is also something to remember about that too is that 50% of the stainless is in flat roll. That is where the hedging is done. On the bar and tube side of the business it is really not, because the quantities are much less than -- flat roll people will hedge because of kitchen equipment manufacturing, projects like that that require a lot of tons.

On the bar side and the tube side of the business, it is really not a big tonnage item. It is a lot of small orders, and that is much less affected by price volatility.

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

And when we are saying hedging, understand that it is not formal hedging. All we are saying is that the customers are buying a little bit more than they probably need at that time. So they are not entering into hedge contracts and all that stuff.

Timna Tanners - ***UBS - Analyst***

Okay, I think I understand. So what you're saying is when things solidified or when nickel seems to be hitting more of a floor to get better visibility on things ramping back up, they might get back into buying more normal now?

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

Yes.

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

Yes.

Timna Tanners - ***UBS - Analyst***

Okay, got it. Last question. I just wanted to understand, the CapEx has been trending really slowly, and I'm just wondering if we still have a target for the end of the year. I thought it was, what, $140 million. I was wondering if that is still good.

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

That is our approved budgeted amount. I don't think there may be one time we hit our budget one year. So are we going to hit it? Probably not. We are at $39 million -- let's say $40 million through the first-half. So we are still continuing, but chances are it might be at about the same rate as the first-half, maybe a little bit --.

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

Yes, we are finishing up some projects. We are building a plant for EMJ in Memphis that will be winding down pretty soon. We are also building another operation for EMJ in Orlando, Florida, which we hope to finish by year-end. We are adding on 150,000 square feet to Yarde Metals in Connecticut. That should be done by hopefully the end of the year. We are also building another large facility for Yarde Metals in Pennsylvania, and that should be wound down in the next few months.

So those are some of the projects -- growth initiatives that we are funding. Again, as Karla pointed out, our Malaysia project just finished up and we're shipping metal out of there now.

Those are the big projects. We've got levelers on order for several of our locations and burning machines and all that other good stuff. But will we hit $140 million? No.

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

Probably not.

Operator

Mark Parr, KeyBanc Capital Markets.

Mark Parr - ***KeyBanc Capital Markets - Analyst***

Great quarter. You guys are awesome. I don't know what else to say.

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

Tell us more, Mark.

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

What did you say, Mark?

Mark Parr - ***KeyBanc Capital Markets - Analyst***

One thing I was curious about, in your third-quarter guidance should we assume a LIFO number somewhere between $7 million and $8 million?

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

Yes, basically it is $15 million for the back half on our current estimate, so it is $7.5 million a quarter.

Mark Parr - ***KeyBanc Capital Markets - Analyst***

Okay, that's helpful. Any shift in mix? Dave, you had mentioned that energy markets are stronger, aerospace markets are stronger. My sense is those may be a little higher margin businesses. Is some improving mix in some of your stronger profit areas perhaps giving you a little more offset in the face of some seasonal weakening?

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

Yes, I think it is. But it takes an awful lot to move the needle, so when we look at it by company we certainly see that. But when you roll it all up into the consolidated numbers, you can see it, but barely, I guess. It takes a lot to move the percentages. But certainly we do get some benefit from those industries that you indicated in really offsetting the weakness in this non-res side.

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

There is some strength, and some of those markets we see strength is also with carbon products, so we expect that to continue to trend up also.

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

Ag equipment in particular is doing very well. Certainly the energy segment and anything related to solar energy we are looking --.

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

Wind.

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

Wind towers. Those are all really just beginning to perk up. We haven't seen a great deal of benefit from it, but we've gotten a lot of quoting activity on it, and we expect to see some benefit in the second-half from that.

Mark Parr - ***KeyBanc Capital Markets - Analyst***

That's really helpful. Another thing I was curious about is you guys have put so much time and energy into the acquisitions that were concluded in '08, prior to the economy collapsing. I am wondering -- here we are, what, almost 2 years later, a year and a half or so later, did you see any good progress with bottom-line performance in some of the recent acquisitions? Or how much more of that could we expect to see over the back half of this year and into '11 that would be independent from just the general market environment?

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

We have seen improvements, thank goodness, from some of the stuff we did in 2008. The big deal that we did then, of course, was the PNA Group. Those six companies together were accretive to us in the quarter, so that is good thing. Are they where we would expect in a more normal type of an economy? No.

I think that you and everyone else out there have not been able to witness the real earnings power of that group of companies. What is it going to take for you to be able to see that impact -- really an improvement in non-res, because most of those businesses in that PNA Group were directly related to non-res construction. They are big in beams and plates and structurals primarily.

So when that picks up then I think you will see a good acceleration for us. We don't know when that is going to be. Probably not this year, but we are hopeful that by -- at least by the back half of next year we should start to see some pickup.

What we are talking more about now, because it is the big unknown, is that private investment in industrial commercial real estate. As Gregg mentioned, we are seeing some good things happening in some of those other areas.

Mark Parr - ***KeyBanc Capital Markets - Analyst***

If I could just ask one more, just a couple of almost housekeeping items. Karla, do you have any idea on the free cash flow outlook for the third quarter? And another question -- are you giving any thought to reviewing the dividend with a sense of perhaps increasing it?

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

On the first item, on the cash flow, given prices -- our expectation that prices will come down a bit and tons would be a moderate improvement or flat, we would expect to generate positive cash flow, maybe fairly consistent with the second-quarter, maybe a little more. Then as far as dividends, certainly that is something that we think about and talk about, and we will be considering.

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

I think what we would like to see -- and as you know, we have consistently raised the dividend, except for, I think, one year in that 2001, 2002 and 2003 period, which was a difficult time, and certainly since this last recession. But what we would like to see, and I think from discussions at the Board level, is just we need to be convinced that there is some real improvement in the economy going on out there.

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

This is Gregg. One thing I did want to point out about the 2008 acquisitions, what has improved there, and there has been substantial improvement in some of those cases, is not a big surprise, but their inventories are turning much, much better than they were and maybe ever have.

Also, their margins have improved certainly over the 2009 period. They're not back to where it is normal, where it should be, but given the fact that they are so non-residential related, we are pretty happy with the progress that they have made. And as Dave pointed out, they are adding to earnings, and thank God for that.

Mark Parr - ***KeyBanc Capital Markets - Analyst***

Terrific. Congratulations on all that progress. And I look forward to talking to you again soon.

Operator

Brett Levy, Jefferies & Co.

Brett Levy - ***Jefferies & Co. - Analyst***

Better than expected quarter. In terms of the acquisitions, can you talk a little bit about what attracts you right now from a product area or geography, whether you're looking outside the box at things like energy, tubular?

Then with respect to the growth strategy, talk a little bit about the Malaysia opportunity and whether or not you're looking at anything that would be a replication of that in other countries. So just kind of two questions.

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

In terms of the type of opportunities that we might be attracted to, we really look at all of the opportunities on their own merits. We do keep an eye on product diversification. Will that particular opportunity make us too heavy in any one product, in any one area? What kind of a customer base does that opportunity have? Are they broad and diverse or is it concentrated in a single type of customer?

We look at all those things, but there is not anything in particular right now that we are on the hunt for. So I guess we will look at every opportunity that is out there, if it seems attractive to us then we will go through the process of thinking through what I just mentioned. But we still prefer bigger deals over smaller deals, but you'll see us do some smaller transactions when there is a strategic reason to do it, or if it can be tucked into one of our existing businesses. So pretty much anything is fair game out there. We will have a look at it, and then make the judgment whether it is attractive to us or not.

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

Maybe from what is attractive, since we didn't really give any -- say a specific geography or product mix is. It is more that a company that is going to be accretive to us. It's profitable at levels that is consistent with our target, is cash flow positive, and has a very strong management team. They've got good customer service, a very good reputation in the industry. Those are the types of things that would make a company attractive to us.

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

Those are all the attributes of the companies that we have acquired, and we wouldn't expect that to change. Certainly the comment Karla just made about accretive to earnings and cash flow positive is absolute, and so that is a necessary part of our thinking process.

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

As far as the Malaysia concern is, we have just opened that up literally. We just started shipping like within the last 30 days. That is an operation that belongs to the EMJ company. We are really following energy over there. So depending on the outcome of our ability to be supported by those energy-related OEM customers, if that is successful, and certainly we believe it will be, because we wouldn't have built otherwise, then if we are pulled to some other operation, whether it be Vietnam or Dubai or wherever it happens to be, we are certainly open-minded to it. It just depends on the support we get.

But all indications are that we are already getting the support that was basically guaranteed to us. So we are hopeful that is going to do very well and then we will just play it by ear and see where it takes us.

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

All of our international expansion has been driven by domestic customer relationships, where those customers have gone into different areas and asked us to come and support them in those areas. So it is less risky, because we can go in, we have a promised or a level of business from this established relationship. And then we use that to build additional business in those areas.

So we don't have any idea about just going anywhere internationally and becoming all things to all people, and trying to be a general line service center somewhere. If you see us go further internationally, it most likely would be because we've got customers and relationships that are asking us to come to those areas and support their businesses there.

The Malaysia operation is pretty exciting for us. It has the potential, and I think all of us expect that that will end up being our largest and most profitable international business -- outside of North America, certainly we have things in Canada, but outside of North America, we think that this Malaysia operation has some real promise.

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

And the Malaysia operation is somewhat consistent with some of our domestic organic growth, where at that location and some other foreign countries we have gone into, as Dave said, with a domestic customer, oftentimes we have already been shipping metal to customers in those countries from the US. So we do have an established customer base and sales base similar to when we do organic growth in those states.

Brett Levy *- Jefferies & Co. - Analyst*

A very complete answer. Just one follow-on; it is small. You guys have got inventory turns that are better than most. As you guys are looking at some of these acquisitions, do you kind of say, well, we can turn them 4.8 times; they can only turn 3.8, so we can buy them, fix them, click, and get an extra quarter of earnings out of each year? Is that somewhat of a template for what you guys look at?

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

Absolutely. I would say of the 45 acquisitions that we have made since becoming a public company in 1994, we have improved the inventory turns and gross profit margin -- well, the inventory turns on 44 of those 45. The other one was turning 12 or 14 times anyway. Then I think 45 of 45 gross profit margins have improved.

Now we were a bit unlucky in mid-2008 because we had a market that turned sour on us soon after an acquisition. But for the most part over the years we have been able to turn things around within, what, 12 months certainly, sometimes a lot quicker than that, depending upon market conditions.

That is what has happened with the PNA companies. It took us a little longer to get their inventories turning and their margins to where we think they should be relative to this market condition. As Gregg said before, that is not normal, but it might be normal for now.

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

Right, right.

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

Even though we always anticipate that we will be able to improve inventory turns and gross profit, we do not put any value for it into our purchase price, so those synergies or benefits belong to Reliance.

Brett Levy *- Jefferies & Co. - Analyst*

Thanks very much guys. Good quarter.

Operator

Richard Garchitorena, Credit Suisse.

Richard Garchitorena *- Credit Suisse - Analyst*

Most of my questions have been answered, but I still have a couple. One is, you mentioned that lead-times are shorter now at the mills. Can you tell us how that trended during the quarter, and how you think that may change in Q3, given the fact we have seen utilization rates come down steadily over the past month?

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

The lead times actually became shorter as the second-quarter progressed. As far as what we think -- what we see in the third quarter, we really don't see any change to the lead times from where they are today. If you are referring to the say flat roll, for example, lead times are anywhere from 4 to 8 weeks. So we don't see that changing any time real soon.

Richard Garchitorena *- Credit Suisse - Analyst*

Then my next question is on non-res construction. Are you seeing any difference among the regions? Are some doing better than others, either on the infrastructure side or the commercial construction side?

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

No. Sorry about that. I wish we could say that one region was picking up and the other couples were not, but really it is very unfortunate, because it is very consistent. It is just tough out there no matter if you are in the Southeast, Northeast, West Coast, non-res is pretty ugly everywhere.

Richard Garchitorena *- Credit Suisse - Analyst*

Okay, that's helpful. Then finally you touched on this earlier, I am just wondering looking out two or three years, if we do get some improvement in the overall economy in the non-res construction, can you remind us what is your peak volume capacity, including the PNA acquisition? Because you look historically those numbers on total volumes don't really reflect that, as you pointed out.

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

Last quarter we gave the number, which was based, I believe, on Q1 2010 volumes. No, 2008 volumes and Q1 pricing. So basically you get to a sales revenue run rate north of $9 billion, given those assumptions.

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

I think when we said last quarter too that was a relatively conservative view of certainly much better conditions, because I think the period that Karla used for pricing was far from the peak and the period she used for the volume assumptions were also far from the peak. On a pro forma basis with 2008 -- now those were certainly peak prices. It wasn't peak volume, but it was certainly peak pricing. We were a bit over a $10 billion pro forma with the PNA transaction as if it had happened on January 1, 2008.

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

That was all the two months of PNA in that quarter, not three.

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

Right, right. So I think what you said last quarter was $9 billion something?

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

Yes.

Operator

Luke Folta, Longbow Research.

Luke Folta - ***Longbow Research - Analyst***

A couple of quick questions just on the aerospace side of your business. Can you give us a feel for how much of your sales went to the aerospace market here in the first-half, ballpark? Then also maybe can you remind us what the real key drivers are there for you as far as which programs you are exposed to?

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

The aerospace revenues -- we have aerospace-related revenues that filter into a lot of our different places. We don't try to pick all of those out, but for the Companies most involved in aerospace, it is about 8%. Maybe slightly less than 8% of our revenue dollars in this last quarter came from aerospace business, our aerospace businesses. We don't go try to pick out order by order out of some of our other businesses that might sell into an aerospace related industry.

Luke Folta - ***Longbow Research - Analyst***

The programs that really drive that for you?

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

The C-17, the F-18, the 747, the 777, those are the major programs.

Luke Folta - ***Longbow Research - Analyst***

I guess I was just trying to get a sense if you guys were seeing any benefit from some of the build rate increases that have been announced, or is that more of a second-half or 2011 phenomenon for you?

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

We are seeing some benefit on the commercial side, but we are not going to see really any -- and I don't even want to use the term significant, but any fairly substantial increases until 2011, 2012. We actually thought 2012 really would mark the time when we would see some pretty good recovery on that. But because of the additional build rates that have been announced that you are referring to now, we are thinking that might move up a little bit into the second-half of 2011.

Luke Folta - ***Longbow Research - Analyst***

The rest of my questions have been answered. Thank you very much.

Operator

Sal Tharani, Goldman Sachs.

Sal Tharani - ***Goldman Sachs - Analyst***

Can you give us an idea on the inventory situation, where do you think it is heading for the next three months? And how are your customers with inventory?

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

Our own inventory?

Sal Tharani - ***Goldman Sachs - Analyst***

Yes. Yours, and what do you think your customers' inventory situation is?

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

I think they are one and the same in that we think that our inventories are going to come down some in the second-half of the year. That is typical for Reliance. We are going to be focusing on that through the balance of the year, so our inventories are going to come down. I think that is fair to say. At least that is what Dave told me last night at the Board meeting that they're coming down. Aren't they, Gregg, I think that was your comment? So that is a given.

On the customer side, they are living hand to mouth. Especially all the prices on all of the products that we have come down in the last few months, whether it is stainless, whether it is aluminum, or any of the carbon steel products. Our customers are aware of that. They did buy a little extra going through basically the first four months of the year. They're not going to be doing that going forward.

Typically our customers realize that prices go down in normal years maybe eight out of ten years in the second-half of the year. So they have been through this cycle as many times as we have, and so they have tightened their belts.

But that doesn't mean that they're not buying maybe even more. If the industries that they support begin to pick up, they are going to have to. But I think we have pretty much, and others, but speaking for Reliance, we pretty much have helped our customers with their inventory and keeping it as low as possible, which helps their banking relationships and whatnot. So they really have been almost addicted to our next day delivery programs, and so they rely on that.

But they're not going to build inventories. They are going to buy it for need, not for greed, just like we are. We would expect our customers' inventory turns probably to be better in the second-half, as we hope ours will be as well.

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

Really, whether the economy is weak, and I guess we would still generally say that the economy is weak overall, or whether it is strong, a normal element of that are price fluctuations in our business. This happened when you're steaming along and maybe the best environment you can imagine, there are still price fluctuations.

If those fluctuations are of the magnitude that we have just seen lately, we don't get too excited about that. That is what we do. We can work through that. That is one of the reasons why through all market conditions, we stress turning inventory. We don't get a little loose when prices are going up, and think that our inventories should be little higher, because you're going to get stung when the prices come down.

What happens is there is too much of a reaction in the marketplace when prices go up or prices go down. It is like there is an overreaction in both directions. And really that is just general business conditions, prices don't go up forever and they don't go down forever. And the unusual thing is what we went through, of course, in late 2008 and first-half at least of 2009 when we had really unusually large price reductions.

But overall this is what we do. It is the world that we live in, and we manage through it. What we would like right now is not necessarily for -- certainly we would like prices to always go up, but that is not going to happen. So if we could just get better demand, I think that would really help us out. We will work through the pricing fluctuations. That is not an issue. But I think there is way too much overreaction on these $20 a ton or $40 a ton price increases and decreases as they occur.

Sal Tharani - ***Goldman Sachs - Analyst***

You mean overreaction to the stock price?

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

Yes, I think reading into it that -- I guess that it is going to impact our business or the service center industry's business in general more. And when prices are going up, I think people get a little too excited on the upside, and when they are coming down they overreact on the downside. This is the world that we live in. Prices go up and prices go down.

I think we have proven that we can manage through those fluctuations, and it is not really worthy of this overreaction that gets put in the marketplace. People try to read the economy when there is a $20 a ton increase. And it is probably nothing to do anything to the economy. And the same on the downside.

The price increases that we had earlier this year, as we have been saying and I think most of you analysts write about, they weren't demand driven necessarily. Certainly there was some demand pickup on the flat roll side, because the auto industry finally woke up and started to improve, and the mills added some capacity because they needed to. But outside of that, the rest of the demand levels were pretty static at low levels. Prices were going up, but not because of demand.

So I think there is just too much read into this daily stuff almost that happens that has an impact, not only on the stock price, but the confidence and the attitude of everybody out there. Sorry for getting on the soapbox there.

Sal Tharani - ***Goldman Sachs - Analyst***

No, that's fine. I want to just talk about a little bit more about aerospace industry. Gregg, you mentioned that there is still inventory overhang. And I believe that you meant aluminum heat-treated plates, and on the other hand I think that is your biggest product you're selling to the aerospace industry. So should we assume that if this overhang is out of the way by the end of the year, you can actually see a further improvement than what you're seeing right now?

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

Yes, that is fair to assume that. That inventory overhang has been around for quite some time. So for us to see some light at the end of the tunnel with respect to that overhang going away, is wonderful in our eyes. There is just too many people are chasing too many orders, because they have too much inventory. We have been very fortunate in that. I won't get into any detail, but we have our inventory turns on the aerospace side -- we are very proud of. But there are others in the industry, I don't believe that can make that statement.

But, yes, when the inventory overhang goes away and supply and demand become more in balance, we would expect our margins to improve. No question.

Sal Tharani - ***Goldman Sachs - Analyst***

Last thing on Morgan City closure, can you give us some color what the basis was? Was that place always struggling or was it just strictly because of the Gulf, which forced you to shut that down?

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

It is really not the Gulf. Well, I guess it is the Gulf, because that is where we are. We are in the Gulf. That facility was constructed prior to Reliance acquiring the Delta Company, which was part of the PNA Group. Their intention was to get into the shipbuilding end of the business. And very honestly, it just never panned out.

I think that we exercised a lot of patience in allowing them to continue to operate that operation, but it was not profitable, it was losing money. There was -- as far as we were concerned, we had a meeting with management, and we said if we weren't in the black by the end of the first-half of the year than we were going to shut it down.

So as it turned out, the oil spill happened and the moratorium on deepwater drilling and all that. But putting all that aside, it didn't make money by the end of the first-half of the year, and we told them we were going to shut it down, and we did.

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

That operation had only been there about four years.

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

Yes. But the only time it ever did -- it wasn't even reasonably well. Because it was fairly new. They got into 2008, prices shot through the roof, demand was tight on carbon steel plate products at the time. They made a little bit of money, but over the course of the four years it really wasn't pretty. And it wasn't because of lack of effort. It wasn't because of poor planning. It is just one of those things that they went into the operation with their eyes open. They took a chance and, you know, you stumble sometimes.

Operator

I am showing there are no further questions in queue.

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

Well, great, I think we are done here. And we look forward to talking to you about three months from now. And I want to remind you again that we are not worried about our own performance. We will continue to grow and we will continue to perform at the top of our industry. Once again, we have tremendous earnings capacity and we're just waiting for the opportunity to demonstrate that as the economy slowly and steadily improves.

So thank you very much. And we will talk to you again in a few months.

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.