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KMG - Q4 2014 KMG Chemicals Inc Earnings Call

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the KMG Q4 2014 earnings conference call. My name is Allison, and I am your operator for today. (Operator Instructions). As a reminder, this call is being recorded for replay purposes.

I'd now like to turn the call over to Mr. Eric Glover, Investor Relations Manager. Please proceed, sir.

Eric Glover *- KMG Chemicals Inc. - IR Manager*

Good morning, everyone, and welcome to the KMG Chemicals, Incorporated fourth-quarter and full-year 2014 financial results conference call. I am joined today by Chris Fraser, our Chairman and CEO, and Mindy Passmore, our CFO. In a moment, we will hear remarks from them followed by Q&A.

During today's call, we will refer to financial measures not calculated according to Generally Accepted Accounting Principles. Please refer to today's earnings release available on our website for the reasons we are presenting non-GAAP financial information and for the appropriate tables of that reconcile these measures to our GAAP results.

Before we begin, I'd like to remind everyone that the information on this conference call includes certain forward-looking statements that are based upon assumptions that in the future may prove not to have been accurate and are subject to significant risks and uncertainties, including statements as to the future performance of the Company.

I will now turn the call over to Chris Fraser, Chairman and CEO. Please go ahead, Chris.

Chris Fraser *- KMG Chemicals Inc. - Chairman, President, CEO*

Thank you, Eric. Good morning and thank you, everyone, for joining us today.

Our Q4 earnings release was issued prior to the market open this morning. After my remarks, I will turn the call over to Mindy for a review of the Q4 and fiscal 2014 financials and our financial outlook for fiscal 2015. After our comments, we will take your questions.

At this time a year ago, I shared our key strategic objectives for fiscal 2014 and our renewed commitment to achieving our full growth potential by intensifying our focus on execution and driving operational efficiencies. Thanks to the efforts of many talented people at KMG over the past year, we've broadened our capabilities and fundamentally strengthened our business. Our fourth-quarter and fiscal 2014 results reflect those efforts.

Fourth-quarter adjusted EBITDA increased to $9 million, up 18% sequentially and 11% year-over-year. Fiscal 2014 adjusted EBITDA improved to $30.6 million, an increase of 4% from the prior year.

Operating cash flow for the year reached a record $40 million, nearly double the level from fiscal 2013. We paid down long-term debt by $25 million, including a reduction of $12 million in the fourth quarter, strengthening our balance sheet and enhancing our financial flexibility.

From an operational standpoint, a top priority in fiscal 2014 was the integration of the UPC business into our global electronic chemicals operations. This acquisition substantially expanded our global footprint and our integration teams performed exceptionally well over the past year, efficiently and effectively integrating the UPC business. KMG is now one global company dedicated to providing the highest level of product quality, reliability, and service to our customers throughout the world.

As part of our integration, we initiated the consolidation of our electronic chemicals operations, which included the closure of our Fremont, California, facility and cessation of manufacturing operations in Milan, Italy. This restructuring will optimize our efficiency, more closely aligning our manufacturing capacity with industry demand for high-purity processed chemicals and will enable us to better serve our customers. The reconfiguration of our manufacturing operations progressed smoothly, remained on schedule throughout the year as we seamlessly transfer production from Fremont to alternate facilities in North America and subsequently initiate the shift to production from Milan to our alternate site in Europe.

Throughout this process, we work closely with our customers to ensure that products involved in these transitions met their stringent quality specifications. Consistent with our original projections, we expect to complete the restructuring of our European operations by the end of calendar 2015, and we expect to realize annualized net benefits to operating income of $6 million to $8 million on an annualized basis.

We continuously pursue opportunities to optimize our businesses and enhance our offering to our customers. As we announced yesterday, we will be realigning our electronic chemicals hydrofluoric acid operations which will reduce our costs and improve our product quality. This initiative enables us to more fully leverage our state-of-the-art Pueblo, Colorado, facility to support purification, packaging, and analytical services for HF, ensuring that KMG continues to meet our customers' future requirements for increasingly pure hydrochloric acid. Starting in fiscal 2016, we expect to realize $1 million to $3 million in annual cost savings from this realignment. Mindy will provide more color in her remarks.

While our electronic chemicals business benefited from improving global semiconductor production trends during fiscal 2014, the creosote demand of our wood treating chemicals business faced less favorable market conditions. In this environment, our focus remained firmly on maximizing cash flow, and we acted to reduce costs in our wood treating business by sourcing lower cost material, rightsizing our supply chain and streamlining our distribution assets. These actions led to cost savings that helped benefit our fourth-quarter results as wood treating chemicals segment's operating margins reached 10.8%, the highest quarter level since Q3 fiscal 2013.

Although headwinds in the creosote market are likely to continue, our penta business performed well in fiscal 2014 and remains an important strategic asset providing consistently solid cash flow. As we look ahead to fiscal 2015, we are optimistic that penta demand will remain strong benefiting from pole replacement programs and the installation of new transmission lines that connect renewable energy sources to the electric grid.

In addition to our efforts to optimize both our electronic chemicals and wood treating chemical business over the past year, we have also taken action at the corporate level to strengthen our internal operations, expand our capabilities, and reduce our overhead costs. First, we commenced the implementation of our global enterprise resource planning system, which will provide the financial system and infrastructure backbone for the Company today and as we grow. Once SAP is implemented throughout our operations we will benefit from a single global platform for financial reporting leading to a more efficient business process and more streamlined integration of future acquisitions. This program remains on budget and on schedule for rollout to our US operations early in calendar 2015.

Second, we have sought to address the escalation in corporate overhead expenses that arose as UPC entities were brought up to the necessary standards for financial reporting and regulatory compliance. Controlling corporate overhead expense remains an important area of focus for us.

Finally, am pleased to report that we obtained a new $150 million credit agreement that expands our borrowing capacity to fund future growth and reduces our annual interest expense significantly. As announced last week, we drew on this facility to retire are 7.43% $20 million term note and refinance the debt drawn on our former facility.

Before I turn the call over to Mindy for the financial review, I would like to offer some comments on market conditions and the outlook for the current fiscal year. Global semiconductor production in calendar 2014 has benefited from relative strength in the mobile and automotive markets. In addition, the personal computer market has shown signs of stabilization in Western Europe and North America aided by increases in corporate IT spending and a pickup in US consumer demand for PCs. Overall, the global semiconductor market is forecast to grow 6% in calendar 2014 according to world semiconductor trade statistics.

Because our electronic chemicals business is closely tied to global semiconductor production, Our EC volumes in calendar 2014 have grown in line with the overall semiconductor market.

From a regional perspective, we have seen good demand in North America and in Singapore while the contraction in the euro zone economy has a limited growth within that market.

Looking ahead to calendar 2015, the global semiconductor market is forecast to grow approximately 3% according to WSTS, representing a deceleration from the projected growth of 6% in calendar 2014. This forecast is consistent with others predicting a more moderate increase in the rate of growth in the global chip market in calendar 2015.

We continue to seek new opportunities for mechanic growth, especially with our global customers who recognize the value in our comprehensive product portfolio, worldwide distribution capabilities and demonstrated ability to meet their increasing need for purity. Over the past year, for example, we expanded our business in Asia and Europe with a leading semiconductor foundry and we gained incremental share in North America with smaller semiconductor manufacturers. In addition, we have increased our participation in faster growth end markets such as mobile, and Internet of Things and remain focused on pursuing these opportunities.

Now, turning to our wood treating chemical segment, we expect to face challenging market dynamics in creosote while penta should continue to perform well. Two primary factors continue to impact our creosote business. As we have discussed previously, the majority of Class I railroads are specifying wood crossties containing borates with a lower level of creosote, which has reduced demand for creosote. Also, the availability of hardwood used for crossties has tightened due to the competing demand from the oil services industry, which uses hardwood for drilling mats. The reduction in hardwood availability combined with Class I railroads preference for borate-treated ties containing less creosote has contributed excess supply and continued downward pressure on prices. In this environment, we continue to be vigilant in our efforts to optimize the supply chain to maximize cash flow.

Meanwhile, the outlook for penta remains positive year in and year out. Penta is a steady performer for us since demand for replacement utility poles remains fairly consistent.

In urban and surrounding areas poles are often replaced prior to reaching their service life for a variety of reasons, including street or road widening projects, accidental damage to poles and upgrades to electrical grid system. From time to time, severe weather can significantly increase regional pole demand, yet this hurricane season remains relatively quiet.

In the Western US, several utilities have increased their replacement budgets as poles approach their useful service life. In addition, as renewable energy sources are connected to electric grid, utilities are opting for penta treated transmission poles that deliver the best combination of value and performance for these applications. As a result, we anticipate that fiscal 2015 will be another solid year for penta sales.

As mentioned in today's earnings release, we will file our Form 10-K for fiscal 2014 next week. The process was more time-consuming than anticipated because of reliance on many manual processes in a significant effort to document internal controls across the UPC entities that were not previously SOX compliant. We do not expect any changes to the financial information in our press release or discussed today.

Although 2014 was a transitional year from a financial standpoint, our adjusted EBITDA results have grown progressive -- have shown progressive improvement over the past three quarters on both a sequential and a year-over-year basis. And we ended fiscal 2014 with our highest level of adjusted EBITDA for the year.

In summary, fiscal 2014 was a pivotal and productive year for KMG. We accomplished several key objectives, including the integration of UPC and streamlining of our global EC operations. We generated record cash flow from operations, strengthened our balance sheet and positioned the Company for long-term growth. We enter fiscal 2015 as a stronger Company, both operationally and financially, and we have built a foundation for growth in the years to come.

Now I'll turn the call over to Mindy for a review the financials.

Mindy Passmore - *KMG Chemicals Inc. - VP, CFO*

Thank you, Chris, and good morning, everyone. In my remarks, I will discuss adjusted or non-GAAP numbers as we believe non-GAAP information can provide useful insight into the underlying operating performance of our business. The non-GAAP numbers I reference are reconciled to the corresponding GAAP numbers in today's earnings release.

I will start with a review of our fourth-quarter results, including an explanation of the charges we took for the restructuring and realignment of our global electronic chemicals operation. I will then review our newly expanded and amended credit facility, which we announced this past Thursday. Finally, I will provide our financial guidance for the fiscal 2015 year.

KMG reported fourth-quarter consolidated net sales of $91.2 million, up 12% year-to-year and up 8% (technical difficulty). The year-to-year sales increase reflected a full quarter's contribution from the acquired UPC business versus two months' contribution in the comparable period last year and organic growth in North America for electronic chemicals. The sequential improvement in sales was due to higher shipment volumes in the electronic chemicals segment.

Gross profit margin in the fourth quarter was 30.7%, up 70 basis points from last year's fourth quarter and 140 basis points from the third quarter of fiscal 2014. Gross profit margins improved year-over-year and sequentially primarily due to higher sales volumes in electronic chemicals as well as cost savings resulting from the restructuring of our North American electronic chemicals operations.

Fourth-quarter distribution expense was $13.3 million versus $10.9 million last year. In dollar terms, distribution expense increased from last year due to the higher level of quarterly revenue. On a percentage basis, distribution expense increased year-over-year to 14.6% in Q4 2014 compared to 13.5% in Q4 2013 due to the UPC acquisition and increased tracking costs in our North American electronic chemicals business.

Fourth-quarter SG&A expense was $9.3 million, down from $10.9 million in the comparable period last year. The majority of this decrease was due to the absence of CEO transition costs in Q4 2014 and lower acquisition and integration expenses. On an adjusted basis, SG&A expenses increased due primarily to increased personnel costs, including stock-based compensation, as we added to our team to expand our internal capability.

Consolidated adjusted EBITDA in the fourth quarter was $9 million, up 11% from $8.1 million in last year's fourth quarter and up 18% from the $7.6 million in the third quarter of fiscal 2014. Fourth-quarter fiscal 2014 adjusted EBITDA excludes $4.5 million of realignment charges at Bay Point and $1.3 million of restructuring charges.

Adjusted EPS for the fourth quarter of fiscal 2014 was $0.27, up from $0.20 in the third quarter of fiscal 2014, but down slightly compared to $0.28 last year. Adjusted EPS increased sequentially primarily due to higher margins in both our business segments. Higher depreciation and amortization expenses and foreign currency exchange losses negatively impacted 2014 fourth-quarter EPS by $0.06 per diluted share versus the comparable period last year.

On a GAAP basis, fourth-quarter fiscal 2014 net loss was $0.07 per share, reflecting restructuring and realignment charges incurred. We reported an income tax benefit of $488,000 in Q4 2014 for a Q4 effective tax benefit rate of 37%. This benefit was primarily due to our net operating loss for the period caused by the Bay Point realignment charges.

Fourth-quarter electronic chemicals sales were $66.3 million, up from $54.3 million last year. The year-over-year increase reflects an additional month of UPC sales as well as higher shipment volumes and improve pricing, particularly in North America.

Adjusted Q4 EBITDA in the electronic chemicals segment was $7.8 million compared to adjusted EBITDA of $6.7 million in last year's fourth quarter. Adjusted EBITDA margins in Q4 improved sequentially.

In our wood treating chemicals segment, Q4 sales were $24.8 million, down from the $26.8 million in the comparable quarter last year. The year-over-year sales decrease primarily reflected lower creosote and hydrochloric acid prices, partially offset by an increase in penta prices.

Wood treating chemicals EBITDA was $2.9 million, or 11.7% of segment sales, versus $2.5 million, or 9.3% of segment sales, in last year's fourth quarter. Segment EBITDA and EBITDA margin benefited from our ongoing efforts to optimize supply chain costs and streamline operating expenses. The $2 million sequential improvement in fourth-quarter adjusted EBITDA for our two business segments was partially offset by increased personnel costs in our corporate segment as we added to our team to expand our internal capabilities.

In the fourth quarter, we incurred $1.8 million in realignment charges for the anticipated closure of Bay Point. These charges included $800,000 for accelerated depreciation of fixed assets that are currently being used in the production of hydrochloric acid and $1 million of decommissioning, decontamination, and dismantling costs.

In addition, we recognized an impairment charge of $2.7 million related to fixed assets that were being held for use and which we have now determined will be disposed of. In fiscal 2015, we estimate incurring realignment charges of $3 million to $5 million, including estimated accelerating depreciation of approximately $2 million. As Chris mentioned, we project annual savings of $1 million to $3 million from this realignment starting in fiscal 2016.

Turning to the manufacturing consolidation of our electronic chemicals operation in North America and Europe, we recorded $1.3 million in fourth-quarter restructuring charges. For fiscal 2014 year, we recorded restructuring charges of $4 million, excluding $2.4 million for accelerated depreciation. Consistent with our prior estimate for $7 million to $9 million in cumulative restructuring charges over fiscal 2014 and 2015, we project restructuring charges for the fiscal 2015 year, excluding accelerated depreciation, will total $3 million to $5 million.

Also, consistent with our prior guidance, fiscal 2015 net benefits to operating income resulting from the restructuring of $6 million to $8 million on an annualized basis are forecast.

Now, turning to the balance sheet, during Q4, we used our strong cash flow to further deleverage, paying down debt by $12 million. For the fiscal 2014 year, we reduced the amount outstanding on our revolving credit facility by $25 million, leaving us with $40 million outstanding on our revolver plus $20 million in term notes as of July 31, 2014. On October 9, we refinanced $20 million of the term note and had $30 million of debt drawn on our former facility with our new credit facility, which features a significantly lower interest rate compared to the rate on the term note. Given this lower rate, we project annual run rate savings from this refinancing of about $1 million.

Now I will review our outlook for fiscal 2015. Fiscal 2015 consolidated net sales are forecast to be essentially flat compared to fiscal 2014 with the likelihood of moderate growth in electronic chemicals offset by potential weakness in our creosote business. Excluding restructuring and realignment charges, fiscal 2015 adjusted EBITDA is forecast to be $32 million to $35 million. Fiscal 2015 depreciation and amortization expense is forecast at approximately $16 million. Fiscal 2015 capital expenditures are forecast at $14 million to $16 million, including expenses related to our ERP system implementation and UPC integration. Our CapEx budget for fiscal 2015 is projected to increase on a year-over-year basis primarily due to ERP project costs and the carryover of integration costs from fiscal 2014.

Operator, please open the call for questions.

QUESTIONS AND ANSWERS

Operator

Thank you. (Operator Instructions). Rosemarie Morbelli, Gabelli & Co.

Rosemarie Morbelli - *Gabelli & Co. - Analyst*

Looking at the electronic chemicals industry, you are expecting a slowdown in 2015 versus the growth rate in 2014. Is that mostly due to slow down in China, slow down in Europe, nothing much happening in Japan, or are there any other reasons? Can you give us a better feel for what is actually happening in the industry?

Chris Fraser - *KMG Chemicals Inc. - Chairman, President, CEO*

Yes, so, we still expect growth, which is what the semiconductor industry is projecting themselves in 2015, just not at the same pace of growth from 2013 to 2014. So, having said that, when we look at our business in particular, we are more heavily weighted in North America and Europe with a smaller percentage being in Asia. The numbers we're looking at show modest growth in North America, somewhat smaller growth in Europe and with a higher growth in Asia, but our business has a smaller percentage in Asia than it does in North America and Europe. So, when we look at our projections going into 2015, we are seeing ourselves pretty much lined up with what the semiconductor industry is saying. So, hopefully, that answers your question, Rosemarie?

Rosemarie Morbelli - *Gabelli & Co. - Analyst*

Yes, no, it helps. In that anticipated growth rate, do you see KMG making bigger inroads into the mobile and other type of applications which are currently small parts of your overall business?

Chris Fraser - *KMG Chemicals Inc. - Chairman, President, CEO*

So, as we have discussed before, it's been an area of focus for us to position our business to take advantage of the higher growth areas, which has been mobile and as well as the potential growth of the Internet of Things. So, we are continually pursuing opportunities with those customers that have a higher growth percentage in those areas. We have seen some improvement in our overall portfolio relative to our share in those areas, and we continue to pursue those. We have made some progress and we are continuing to go along those lines.

In addition, as I mentioned, we are working with the global customers who get benefits from us being in and having a presence in three continents, and working with them from a global perspective and supplying and having them source from us in multiple locations.

Rosemarie Morbelli - *Gabelli & Co. - Analyst*

Okay, no, that is helpful. I was wondering. With the consolidation of the manufacturing facilities regarding UPC and so on, what kind of capacity utilization are you operating in now?

Chris Fraser - *KMG Chemicals Inc. - Chairman, President, CEO*

So, we haven't typically given that number out. Let's just say we are very comfortable with our capacity utilization today and our ability to grow with the market. Even though we have consolidated operations, we still have room to take on additional growth and feel good about optimizing the assets that we have.

Rosemarie Morbelli - *Gabelli & Co. - Analyst*

Okay, that is helpful. And if I may ask a couple other questions before I pass it on. On the wood side, what else can you do in order to increase profitability further, increase those in line with -- well, yes, let's say in line with the slower demand or shrinking demand, which seems to be continuing to shrink?

Chris Fraser - *KMG Chemicals Inc. - Chairman, President, CEO*

Yes, so, we don't control demand, nor do we control supply, so, we're in a situation where it's an oversupplied market and it continues to be very competitive and we are seeing, with that oversupplied situation, continued reduction in pricing. So, we are looking and working hard on all the aspects of costs that we can control, which is our supply chain, optimizing that, making sure we have the right fleet size to serve our customers but not be over-fleeted in railcars, for example, to make sure we have the right amount of storage, not in excess, and just right-size our overall supply chain.

In addition, we are continually looking at reducing our costs of creosote supply and doing everything we can to optimize those as well to make sure we are as competitive as possible in that market. But we do see that competitive pressures continuing into 2015 as we saw in 2014. We, at this point, are not seeing any relief on that competitive pressures and we want to make sure we call that out and identify that.

Rosemarie Morbelli - *Gabelli & Co. - Analyst*

Okay. And then lastly, if I may, on the SAP rollout, this never goes smoothly. Are you anticipating any issues in the first half of next year when you roll it out, or do think that you are set up in such a way that it could go smoothly as opposed to just about everybody else?

Chris Fraser - *KMG Chemicals Inc. - Chairman, President, CEO*

Yes, that's a great question. So, here we are in mid-October. We're going live February 2, and the team is on schedule. The project is within the budget as we outlined. We're moving into the next phases of training as well as getting more of the organization involved in the expected kickoff. So at this point, Rosemarie, we are feeling comfortable with our plan and being able to meet those, the timelines that we have put forth. So, we've got a really good team, some really good leaders working on that project, and we are comfortable and confident that we will be able to deliver it on time.

Rosemarie Morbelli - *Gabelli & Co. - Analyst*

Okay, thanks much.

Operator

Jay Harris, Axiom Capital Management.

Jay Harris - *Axiom Capital Management - Analyst*

I wondered if you could share with us the -- had you owned the UPC business for 12 months instead of 11 months, how much of the revenue gain aggregately was due to volume and how much was due to price?

Chris Fraser - *KMG Chemicals Inc. - Chairman, President, CEO*

Okay, so, let me make sure I understand your question. How much of the UPC business?

Jay Harris - *Axiom Capital Management - Analyst*

No, your electronic business adjusted for -- with the 12-month included. In other words, you only had UPC for 11 months.

Chris Fraser - *KMG Chemicals Inc. - Chairman, President, CEO*

Right.

Jay Harris - *Axiom Capital Management - Analyst*

Had you owned it for 12 months, what would have been the volume growth rate in the business and how much of the revenue gains were due to price changes?

Chris Fraser - *KMG Chemicals Inc. - Chairman, President, CEO*

Yes, so, don't have that specifically broken down into those, but what I can give you from a volume standpoint and an overall revenue standpoint, as I said earlier, we are tracking with the industry. The industry perspective of growth, 6% calendar year over calendar year, and our revenue is tracking with that. We have had some price improvement and our volume is in line with what we see the overall production levels.

Our regional mix is slightly different than the overall global, but we feel very comfortable that we are in line, in fact tracking in some areas better than what the projections were. So, I don't have the specific breakdown for you, but feel really good that we are tracking with the industry perspective.

Jay Harris - *Axiom Capital Management - Analyst*

I was shooting for the equivalent of an organic growth rate, but okay. Can you comment on the seasonality of the electronics business?

Chris Fraser - *KMG Chemicals Inc. - Chairman, President, CEO*

Sure. So, typically the third quarter is typically one of the strongest quarters, and we are seeing that today with the continued growth, as we outlined earlier. So, this, the quarter, the calendar third quarter is typically one of the strongest, and we are seeing that today, specifically in North America. Europe is not growing as fast as we would have liked, but that's a reflection of the eurozone, but, again, more in line with what the overall semiconductor projections are for each region.

Jay Harris - *Axiom Capital Management - Analyst*

If you are looking for a modest increase in electronics chemicals revenues in your current fiscal year, which quarter would be the low quarter?

Chris Fraser - *KMG Chemicals Inc. - Chairman, President, CEO*

The low quarter is typically our second fiscal quarter.

Jay Harris - *Axiom Capital Management - Analyst*

Thank you.

Operator

[Eric Preity], Hudson.

Eric Preity - *Hudson Square Research - Analyst*

You guys did a great job paying down your debt this quarter. Do you have an optimal capital structure that you're shooting for or are you going to pay the revolver more or less down to zero as you continue to generate cash flow?

Mindy Passmore - *KMG Chemicals Inc. - VP, CFO*

Yes, we are continuing to look at our capital structure and our focus has been paying down the revolver. We did, as you know, get a new revolving credit agreement the has an increased capacity in anticipation of potential acquisitions.

So going forward, considering again our stock price as well as the interest rates, we're going to continue to evaluate options on capital structure also in line with what potential acquisitions might be out there.

Eric Preity - *Hudson Square Research - Analyst*

Okay, yes, so it sounds like you are considering acquisitions and buybacks potentially to also -- for uses of cash?

Mindy Passmore - *KMG Chemicals Inc. - VP, CFO*

Everything is on the table to maximize shareholder value.

Eric Preity - *Hudson Square Research - Analyst*

Great. And then just a follow-up to some of the electronic chemicals questions out there. There is some good news coming out of the industry. Are you expecting, say, the strength that we are seeing now out of the Intels and the Microns of the world to diminish as the year continues, or are you and the industry expecting continued strength throughout the year?

Chris Fraser - *KMG Chemicals Inc. - Chairman, President, CEO*

The strength that we are seeing we expect to continue through calendar 2014 in line with what they have been saying. There has not been a lot -- they have not given a lot of guidance into 2015 at this point, so our projections for 2015 are more in line with the overall semiconductor industry, but we do expect to see the continued strength through calendar 2014.

Eric Preity - *Hudson Square Research - Analyst*

Then a follow-up to some of the questions on capacity in electronic chemicals. You do see that business ramping up this year. What type of margins, incremental margins, are you seeing in that business? Is there enough latent capacity where you are getting significantly higher margins as you increase your volumes through the plant?

Chris Fraser - *KMG Chemicals Inc. - Chairman, President, CEO*

Yes, our overall strategy is to fully utilize our assets so, the obvious benefit is, as the assets are more fully employed, we get the benefit of further fixed cost coverage and therefore higher margins. So, yes, we do anticipate that and that's part of our savings that we've put forth in our synergies is those better utilization of the assets as we drive towards the consolidation.

Eric Preity - *Hudson Square Research - Analyst*

Okay, great. One final question. You might have mentioned this already in your discussion with creosote, but where are you from a supplier standpoint and is there opportunities for either additional suppliers or lower cost suppliers, and where would you be in some of those conversations?

Chris Fraser - *KMG Chemicals Inc. - Chairman, President, CEO*

Yes, so it's something we continuously look at. As a distributor of creosote in North America, we have multiple sources, and we continuously look at other alternatives to bring in material at the lowest, most optimal cost possible. So, it's something we have made some progress on, and we continue to look at other options that can provide us low-cost material.

Eric Preity - *Hudson Square Research - Analyst*

Great, okay, thank you very much.

Operator

Rosemarie Morbelli, Gabelli & Co.

Rosemarie Morbelli - *Gabelli & Co. - Analyst*

Just quickly, Mindy, could you give us a feel as to where the strong cash flow generation came from? Can you talk about the working capital, what you are working on and what needs to be -- what remains to be done?

Mindy Passmore - *KMG Chemicals Inc. - VP, CFO*

Sure. So, the strong cash flow, of course, came from the strong EBITDA, so that's one thing. But also in addition to that, we have significantly improved our cash conversion cycle, particularly in Q4. Really, management has had a real focus on inventory management. Some of the improvement I would say in the operating cash flows is probably timing, because, as you probably know from the past, creosote purchases and shipments come in and large dollar chunks, so some of that is due to that being down, but some of it is also, I believe, sustainable because of the focus on working capital management. And to that end, again, one of the big objectives of our SAP project is to provide the tools so that operations can see supply and demand and better manage working capital as well.

Rosemarie Morbelli - *Gabelli & Co. - Analyst*

Okay. Are you satisfied with your inventory level at this point?

Mindy Passmore - *KMG Chemicals Inc. - VP, CFO*

I'm never satisfied.

Rosemarie Morbelli - *Gabelli & Co. - Analyst*

Okay, so we will see more to come.

Mindy Passmore - *KMG Chemicals Inc. - VP, CFO*

That's the goal.

Rosemarie Morbelli - *Gabelli & Co. - Analyst*

Okay, thank you very much.

Operator

Richard O'Reilly, Revere Associates.

Richard O'Reilly - *Revere Associates - Analyst*

On the original electronics restructuring, how much do you think you realized in fiscal 2014 of those savings?

Chris Fraser - *KMG Chemicals Inc. - Chairman, President, CEO*

Go ahead, Mindy.

Mindy Passmore - *KMG Chemicals Inc. - VP, CFO*

We believe we realized about a $1.5 million in fiscal 2014.

Richard O'Reilly - *Revere Associates - Analyst*

Okay, so the delta in 2015 will be that $6 million to $8 million minus the $1.5 million that you realized in 2014?

Mindy Passmore - *KMG Chemicals Inc. - VP, CFO*

No, fiscal 2015, as Chris mentioned, is -- the restructuring in Milan is going to take well into the full 2015, so the $6 million to $8 million, and we've said this in the past, is that annual run rate that we expect to achieve towards the back half of fiscal 2015. So, the incremental savings in fiscal 2015 to fiscal 2014 will not be as much as that.

Richard O'Reilly - *Revere Associates - Analyst*

Okay, fine. Okay, I misunderstood that, okay. Second question, a bigger question, Chris. Do you talk about margin goals for the electronics business? Because generally it has been running even below the chemical business, the wood treatment business. Do you talk about what type of goals you want for that business, the electronic business?

Chris Fraser - *KMG Chemicals Inc. - Chairman, President, CEO*

Yes, we do a lot of talking about that internally. It's not something that we have been externally talking about, but it's an area of focus for us. We provide a lot of value to our customers and we provide a lot of services for them. And there is a clear focus from us to improve our margins and both from making sure we get the return for the investments we are making in our capabilities as well as making sure we get the benefits from the customers in providing them all the values that we do. So, it's a keen focus internally, and we are seeing some margin improvement partially because of our cost improvements, but also we have been able to successfully get some price improvements. And as we become a bigger global supplier and more -- as a more valued supplier across the globe, we will continue to look for improvements in those areas overall.

Richard O'Reilly - *Revere Associates - Analyst*

Okay. I won't be able to get you to quantify anything today, right?

Chris Fraser - *KMG Chemicals Inc. - Chairman, President, CEO*

No, but thanks for asking. But let's just say it's an area of focus for us and something we are continuing to drive forward.

Richard O'Reilly - *Revere Associates - Analyst*

Okay, thanks a lot, thanks a lot for answering the questions.

Operator

Jay Harris, Axiom Capital Management.

Jay Harris - *Axiom Capital Management - Analyst*

As you look ahead towards fiscal 2016, how do you expect your tax rate to change?

Mindy Passmore - *KMG Chemicals Inc. - VP, CFO*

That is going to depend on, obviously on the distribution of income between US and foreign jurisdictions because the tax rates vary. But that said, I would say, currently, we are expecting the tax rate just for in general to be around 30%, excluding restructuring, I mean the restructuring of Milan impact to be on a consolidation about 30% to, say, 32%.

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Jay Harris - *Axiom Capital Management - Analyst*

Wouldn't it be lower in 2016 than 2015 everything else being equal?

Mindy Passmore - *KMG Chemicals Inc. - VP, CFO*

Not following. Why do you say that?

Jay Harris - *Axiom Capital Management - Analyst*

I should have phrased it as more of a question rather than a statement. I'm sorry. In other words, I guess your question to me suggests that you don't think that the geographic distribution of earnings are going to change very much over the next two years.

Chris Fraser - *KMG Chemicals Inc. - Chairman, President, CEO*

At this point, we are not anticipating that changing.

Jay Harris - *Axiom Capital Management - Analyst*

All right. That gives me the answer then. Thank you.

Operator

Thank you. I would now like to turn the call over to Chris Fraser for closing remarks.

Chris Fraser - *KMG Chemicals Inc. - Chairman, President, CEO*

We appreciate everyone's participation today and your interest in KMG, and we look forward to speaking with you on our first-quarter fiscal 2015 conference call. Thank you.

Operator

Thank you for joining today's conference call. This concludes the presentation. You may now disconnect. Good day.