THOMSON REUTERS STREETEVENTS

EDITED TRANSCRIPT

RS - Q4 2015 Reliance Steel & Aluminum Co Earnings Call

EVENT DATE/TIME: FEBRUARY 18, 2016 / 4:00PM GMT

OVERVIEW:

Co. reported 4Q15 non-GAAP net income attributable to Co. $63.3m or $0.87 per diluted share. Expects 1Q16 non-GAAP diluted EPS to be $0.80-0.90.

CORPORATE PARTICIPANTS

Brenda Miyamoto *Reliance Steel & Aluminum Company - IR*

Gregg Mollins *Reliance Steel & Aluminum Company - President & CEO*

Jim Hoffman *Reliance Steel & Aluminum Company - EVP, Operations*

Bill Sales *Reliance Steel & Aluminum Company - EVP, Operations*

Karla Lewis *Reliance Steel & Aluminum Company - Senior EVP & CFO*

CONFERENCE CALL PARTICIPANTS

Timna Tanners *BofA Merrill Lynch - Analyst*

Phil Gibbs *KeyBanc Capital Markets - Analyst*

Michael Gambardella *JPMorgan - Analyst*

Aldo Mazzaferro *Macquarie Research - Analyst*

Chris Olin *Cleveland Research Company - Analyst*

PRESENTATION

Operator

Greetings and welcome to the Reliance Steel & Aluminum Co. fourth-quarter and full-year 2015 earnings conference call.

(Operator Instructions)

As a reminder, this conference is being recorded. I would elected to the conference over to your host, Brenda Miyamoto with Investor Relations. Thank you, you may now begin.

Brenda Miyamoto - *Reliance Steel & Aluminum Company - IR*

Thank you, operator. Good morning and thanks to all of you for joining our conference call to discuss our fourth-quarter and full-year 2015 financial results.

I am joined by Gregg Mollins, our President and CEO, Karla Lewis, our Senior Executive Vice President and CFO, and our Executive Vice Presidents of Operations Jim Hoffman and Bill Sales. David Hannah, our Executive Chairman, will also be available during the question-and-answer portion of this call. A recording of this call will be posted on the investor section of our website at Investor. RSAC.com.

The press release and the information on this call may contain certain forward looking statements, which are based on a number of assumptions that are subject to change and involve known and unknown risks, uncertainties, or other factors which may not be under the Company's control which may cause the actual results, performance or achieving of the company to be materially different from the results performance or other expectations implied by these forward-looking statements. These factors include but are not limited to those factors disclosed in the Company's annual report on Form 10-K for the year ended December 31, 2014 under the caption risk factors and other reports filed with the Securities and Exchange Commission. The press release and the information on this call speak only as of today's date and the Company disclaims any duty to update the information provided therein and herein.

I'll now turn the call over to Gregg Mollins, President and CEO of Reliance.

Gregg Mollins - *Reliance Steel & Aluminum Company - President & CEO*

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

We were very pleased with our strong operational execution throughout 2015 despite a very challenging economic environment that continued pressure metal pricing. We finished the year generating record cash flow from operations of $1 billion which affords us ample liquidity and financial flexibility to continue to execute on all of our capital allocation priorities. We were successful in reducing inventory, a key area of focus for Reliance in 2015, by an additional $193.3 million during the fourth quarter and $433.1 million for the year. We increased our fourth-quarter FIFO gross profit margins to 26.7% up 30 basis points from the prior quarter and up 160 basis points from the fourth quarter of 2014. I am pleased to report that we were able to increase our gross profit margin in each successive quarter for 2015 during a period when metal pricing declined in each successive quarter. An impressive accomplishment made possible by the outstanding quality people that we have throughout Reliance.

In addition to our focus on smaller order sizes and next day delivery, we believe that our increased investments and value-added processing, as well as efficiently managing our inventory, contributed to our increase gross profit margins. The amount charged for processing services does not fluctuate with metal pricing so as a metal prices fall, the value added component becomes a larger portion of the total selling price. In addition, we strongly believe that maintaining the right level of inventory to support current sales activity at each of our operations encourages local management to turn away low margin business and focus on higher-margin orders. If you have too much inventory, it's easy to take a bad order. We prefer higher profit over volume.

Mill prices were many of our products ended the year down 30% to 40% compared to the beginning of the year due to continued high levels of imports flooding the US market resulting from a strong US dollar and the weak global economy. These factors caused US steel producers to file trade cases for most flat-rolled carbon steel products in the second half of 2015. We support these trade actions and it appears the pending actions have reduced imports somewhat prompting the domestic mills to announce moderate price increases on almost all carbon steel products so far in 2016.

During the fourth quarter, both demand and pricing were softer than we had anticipated. We had expected fourth quarter pricing to be down 1% to 2%. However, conditions continued to soften throughout the quarter resulting in our average selling price per ton sold declining 4.5% compared to the prior quarter and 16.6% compared to the fourth quarter of 2014.

We had also anticipated slightly stronger demand than normal for the fourth quarter in our guidance of down 4% to 5%. However, due to the normal seasonal slowdown from fewer shipping days as a result of the holidays and holiday related closures by many of our customers, coupled with the slumping energy market and ongoing concerns over slowed growth in China, our tons sold were down 7.1% from the prior quarter and 6.1% compared to the fourth quarter of 2014. Nevertheless, demand trends for many of the industry's we support held up relatively well throughout the year and we once again outperformed the MSCI industry average decline of 10.1% for the fourth quarter. We also out paced the industry for the full year of 2015 compared to 2014 with the 2.8% decline in our tons sold compared to the MSCI industry average decline of 7.5%. Tons sold by our energy businesses were down 41% in 2015 from 2014 levels. Excluding the impact of the energy downturn, our tons sold for 2015 were down a mere 0.7% from 2014.

We've been able to grow our market share in this challenging environment by staying the course with our tried-and-true business model that emphasizes a decentralized structure and places the day-to-day sales decisions in the hands of our managers in the field. Our managers have built strong customer relationships over the years and have the ability to fulfill quick turnaround orders, often in 24 hours or less, for customers looking to place orders for smaller quantities on a more frequent basis, especially when metal prices are declining.

In addition, we have made and will continue to make significant investments in the strongest areas of our Company currently being those businesses servicing aerospace customers as well as in the automotive industry mostly through toll processing. Because of the high-volume processing performed by our toll processing businesses, they are more capital intensive than other parts of our business making it important for us to regularly invest in our processing equipment to ensure state-of-the-art capabilities as well as to capitalize on the recent growth in aluminum processing. We have also invested to expand our footprint in the aerospace market through our August 2014 acquisition of Aluminum Services UK Limited and the opening of additional new facilities around the globe in anticipation of continued strong demand in this important market. Despite the industry wide challenges, we remained focused on our key initiatives in 2015 which were aimed at reducing inventory, managing our gross profit margin and operating expenses and growth through M&A and organic activity.

In 2015, we decreased our FIFO inventory by $433.1 million including $193.3 million during the fourth quarter. As a result, our inventory turn rate was 5.2 times based on inventory tons on hand at December 31, 2015 and our full-year 2015 shipment levels, which is well ahead of it company wide goal of 4.75 times. By converting inventory to cash, we were able to further reduce our debt balance by $167.5 million during the fourth quarter and repurchased $13.2 million worth of our outstanding shares.

Turning to M& A, effective January 1, 2016 we acquired Tubular Steel Inc. A distributor and processor of carbon, alloy, and stainless steel pipe, tubing and barb products based in St. Louis, Missouri. Tubular Steel is a strong company with a well respected position in the market. Tubular Steel brings additional high margin, specialty products to our mix and fits our growth strategy of investing in higher returning businesses while expanding our product breadth and end market diversification. We continue to evaluate various opportunities as part of our overall growth strategy to acquire profitable, well-managed metal service centers and processors with product and end market exposures that help support our diversification strategy.

In summary, despite the challenges we face in our industry at large, I am very pleased with our full-year 2015 performance which reflected superior operational execution. We generated record cash flow from operations of $1 billion. We increased our FIFO gross profit margins to 26%, we reduced our inventory by $433.1 million. We paid down $376.6 million of debt and we repurchased $355.5 million of our common stock. I'm very proud of the entire Reliance team and all they have accomplished throughout this otherwise challenging year. Our strong operational execution enabled us to continue growing our market share and gross profit margins as well as generate significant cash to execute on our growth strategy and shareholder return priorities. Our balance sheet remains solid and affords us great flexibility to continue growing our business while at the same time returning capital to our valued shareholders in the form of quarterly cash dividends and opportunistic share repurchases as well as being in a position to further deleverage our balance sheet. We're optimistic for the year ahead and look forward to building upon our operational momentum.

I'll now hand the call over to Jim to comment further on our operations and market conditions. Jim?

Jim Hoffman - *Reliance Steel & Aluminum Company - EVP, Operations*

Thanks Craig and good morning everyone.

Our comments today will focus both on pricing and demand for our carbon steel and alloy products, as well as our outlook on certain key end markets we sell those products into. Including automotive, heavy industry, nonresidential construction and energy. Bill will then address our aluminum and stainless steel products and related end markets.

Demand for automotive which we service mainly through our full processing operations in the USA and Mexico was strong throughout the year, a trend we expect to continue in 2016. In light of this we are expanding two of our existing facilities as well as constructing a new facility in Mexico and one in Kentucky. The new facility in Mexico will increase our existing toll processing capacity to support the increased automotive activity there and is expected to begin operating in mid-2016. Will also begin construction on a new facility in Kentucky to support our growing aluminum toll processing business. Reliance has been very successful in establishing itself through its Precision Strip Inc. subsidiary, a toll processor of aluminum used in the US automotive industry, a fast-growing market.

We believe that our success in toll processing metal for the automotive end market is due to our high quality, internally engineered processing equipment allows us to handle both steel and aluminum products that meet the high-quality standard for exposed products. With the sudden and significant increase in aluminum used in autos, Reliance is one of the few toll processing companies that has the funds available to support this growth. For example, in 2015, we opened a new facility and installed state-of-the-art equipment which is fairly expensive. That allowed us to process two times the volume of aluminum we processed in 2014 at our toll processing operations. At Reliance, we are particularly fond of this business. As we take on no inventory risk so our toll processing operations are not impacted by metal pricing. We simply process the metal for a fee without taking ownership of it. As we've mentioned in the past, although toll processing represents a small portion of our total sales dollars, it represents a larger percentage of our profitability.

Turning to heavy industry, which includes railcar, truck trailer, shipbuilding, large manufacturing, tank manufacturing and wind and transmission towers, demand in the fourth quarter remained fairly consistent with prior quarter levels subject to the normal fourth quarter seasonal slowdown. Our exposure to heavy equipment also includes sales to agricultural equipment OEMs. While demand for large agricultural equipment has been weak, Reliance's exposure is mostly to small and midsize agricultural equipment which is held up better than the heavier items. On a positive note, demand in the road construction equipment market is trending up and is poised to increase in 2016 as a result of the five-year infrastructure bill that was passed in December 2015.

Demand in our largest end market, nonresidential construction, improved in 2015 from 2014 levels yet are volume remains well below peak levels. We expect that demand will continue to improve in 2016 and beyond. We sell many different products into the nonresidential construction market and rather than scaling back our footprint or closing facilities that service this market due to the 2009 downturn, we have been strategically investing in processing equipment to allow us to do even more for our customers as this end market improves. As a result, we are very well-positioned in this market with capacities to absorb volumes increases in our existing cost structures.

Turning to energy. That being mainly oil and natural gas, both volume and pricing continue to deteriorate in the fourth quarter due to continued declining oil prices and related reduction in drilling activities. As a result, our energy-related volumes were down 41% in 2015 compared to 2014 and down 51% in the fourth quarter of 2015 compared to the fourth quarter of 2014. We've been very proactive in reacting to the decline in demand. We began cutting expenses within our energy-related service centers over a year ago and our operating expense run rate for these businesses is now approximately 35% lower than it was at the end of 2014. This has helped mitigate the negative impact to Reliance's overall profitability. Our outlook for energy end market remains weak for the foreseeable future. As such, we made further headcount reductions at our businesses servicing the energy market during the fourth quarter resulting in a reduction of 466 employees for about 36% for the full year of 2015.

Turning to pricing. We experienced further decline in carbon steel pricing in the fourth quarter. Although there has been some success in trade cases filed in the US, there was little direct impact during the fourth quarter. However, we have begun to see some improvement in carbon steel pricing in the first quarter of 2016. While demand for carbon steel products is holding up, the continued pressure on pricing from high import levels into the marketplace, low raw material prices, a strong US dollar, and a soft global economy including a weak Chinese market, limits the effectiveness of trade cases. That said, we're very pleased we were once again able to increase our FIFO gross profit margin on sales of our carbon steel products in the 2015 fourth quarter.

Among carbon steel products, plate represents the largest portion of our product mix at 12% of our total sales followed by carbon steel structurals, tubing, and bars. As such, our results are more heavily impacted by pricing on these products versus carbon flat-rolled products which represents only 15% of our total sales with hot-rolled at 7%. Flat-rolled pricing was under pressure for the entire 2015 year with the mill prices down over 30% compared to the beginning of 2015. Though plate demands remains fairly healthy, pricing for plate products declined significantly, down more than 40% from the beginning of 2015. Base prices for alloy products the majority of which are sold into the energy end markets have held up well considering the significant reduction in demand. Going forward, we expect prices for these products to remain fairly steady with current levels due in large part to alloy products going into the automotive market.

Now I'll hand the call over to Bill to comment further on our nonferrous markets. Bill?

Bill Sales - *Reliance Steel & Aluminum Company - EVP, Operations*

Thanks Jim. Good morning everyone.

I'll begin with aerospace which continues to be one of our strongest end markets for us due to its relatively stable pricing and strong demand trends. Sales to the aerospace market represented approximately 10% of our total sales in 2015. Our same-store tons sold to the aerospace market were up 10.4% for the 2015 year compared to 2014. Demand in this market continues to be strong with healthy build rates in the commercial airline market tied to record aircraft deliveries in 2015 and a robust backlog. Over the past couple of years, we have been purposely increasing our aerospace exposure on a global basis consistent with our customers growth patterns. We have been successful in gaining market share through facilities expansion as well as through successful M&A activities.

I'm pleased report that earlier this month we were awarded $100 million contract by BAE Systems to provide aluminum plate to support the F-35 joint strike fighter Hawk and Typhoon programs. This five-year contract runs from 2017 through 2021 with the possibility of additional years. This contract is in addition to an award by Lockheed Martin in October of 2015 to provide aluminum products and services for the F-35 program and a five-year contract valued at an estimated $300 million.

The majority of the products that we sell to the aerospace market are heat-treated aluminum products, especially plate as well as specialty stainless steel and titanium products. Given continued strong demand, we expect pricing for aluminum aerospace plate to be stable through the first half of 2016. Lead times from the domestic mills remained extended at 25+ weeks. Our sales of common alloy aluminum remain consistent from a volume standpoint with most of our product being sold to sheet metal fabricators that support a variety of end markets. Demand for general engineering aluminum plate remains stable yet pricing continues to be challenged due to ongoing aggressive import pricing. Demand is expected to remain steady through the first half of 2016.

Pricing on common alloy aluminum sheet follows ingot and we expect some modest improvement as the Midwest spot prices trends up slightly. Midwest spot ingot has been trading in the $0.77 to $0.79 per pound range down from $1.06 per pound in January 2015 but up from the $0.75 per pound average for December 2015. The Midwest premium is currently in the $0.096 per pound range.

Outside of the energy markets demand for stainless steel products has continued to be good despite a very challenging pricing environment in 2015. Primarily related to stainless flat-roll. Pricing for flat-roll stainless steel products has declined about 35% from the beginning of 2015. Pricing per stainless steel flat-rolled products increased modestly in early 2016 based on a January increase, another increase was just announced for March and we believe it will have market support. In addition, the recently announced trade case petition for stainless steel sheet and strip, against imports from China, should lessen the flow of Chinese imports to the US and the negative impact on market pricing. We sell a significant amount of stainless steel flat-rolled products into the kitchen equipment, appliance and construction end markets.

Pricing for all of these products is heavily impacted by nickel prices which declined through most of 2015 and have continued to decline so far in 2016. The monthly average nickel price for January was $3.93 per pound. Last week nickel prices dipped below the $3.50 per pound. A level we haven't seen since 2002. Surcharges for 304 stainless fell from $0.76 per pound in January 2015 to $0.33 per pound in January 2016. While we expect prices for stainless steel products to remain under pressure in 2016, we believe we may be at or near the bottom of this cycle. Despite the challenging pricing environment, our managers in the aluminum and stainless steel portions of our business have maintained healthy gross profit margins and have simultaneously managed their expenses well. We applaud them for their efforts.

I now turn the call over to Karla to review our fourth-quarter financial results.

Karla Lewis - *Reliance Steel & Aluminum Company - Senior EVP & CFO*

Thanks Bill, and good morning everyone. Our sales in the fourth quarter of 2015 were down $550.5 million or 21.4% from the fourth quarter of 2014 and down $260 million or 11.4% from the third quarter of 2015. For the 2015 year, our sales were down $1.1 billion or 10.5% from 2014 mainly due to lower metals pricing with our 2015 average selling price per tons sold down a 8.6% from 2014. Our same-store average selling price has declined sequentially in each month beginning in September 2014 until December 2015 when we saw a very slight increase for the first time. However, our December 2015 same-store average selling price was down $314 per ton or 18.1% from our September 2014 average selling price.

Based on our 2015 tons sold and a FIFO gross profit margin of 26.0%, this equates to a loss of nearly $1.86 billion of annual sales and $483 million of gross profit due solely to the impact of metals pricing. We recorded a net LIFO inventory evaluation credit or income of $117 million in 2015. Because of the significant declines in metal prices, we used up our beginning of the year LIFO reserve and recorded a lower of cost to market charge of $69.1 million because our LIFO inventory cost on hand at December 31, 2015 was higher than replacement costs resulting in a year-end net reserve of $26.1 million. As a result, our net LIFO adjustment for the 2015 fourth-quarter was a credit or income of $42 million or $0.35 per share which was included in our cost of sales. This is compared to a charge or expense of $24.5 million or $0.19 per share in the 2014 fourth quarter. And in the 2015 third quarter, we had a net LIFO credit or income of $35 million or $0.29 per share. Our 2015 full-year LIFO adjustment was a credit or income of $186.1 million partially offset by a $69.1 million charge to record LIFO inventory at the lower of cost market for a net credit or income of $117 million or $0.97 per share compared to a 2014 charge for expense of $54.5 million or $0.43 per share.

At this time, we anticipate that 2016 metal prices will be flat to up slightly from 2015 levels. If prices increase, we anticipate a LIFO charge or expense in 2016. At the end of each quarter, we will also update our lower of cost or market reserve. If metal prices increase, we anticipate a decrease in the reserve or income that would be netted against the LIFO charge. Based on this, we currently do not anticipate a LIFO adjustment for 2016. And as in prior years, we will update our expectations quarterly based upon our inventory costs and general metals pricing trends.

Our 2015 fourth-quarter gross profit margin of 28.7% increased from 24.2% in the 2014 fourth quarter and 27.9% in the 2015 third-quarter. Our increased LIFO income contributed to our higher gross profit margin. On a FIFO basis, our gross profit margin during the quarter increased for the fourth consecutive quarter exceeding our expectations especially in light of the declining prices. Our 2015 fourth-quarter SG&A expenses decreased $18.3 million from the 2014 fourth quarter and $16.2 million from the 2015 third-quarter primarily due to a nonrecurring credit of $8.6 million from proceeds received from a mill antitrust settlement as well as effective cost control throughout the Company. As a percent of sales, our SG&A expenses were 20.4% compared to 16.7% in the 2014 fourth quarter and 18.8% in the 2015 third quarter. The increase as a percent of sales was impacted mainly by lower selling prices in the 2015 fourth-quarter. If we apply our 2014 average selling price to our 2015 fourth-quarter results, our SG&A expense as a percent of sales would have declined to 17.0% of sales.

As Jim mentioned, during 2015 we had significant reductions in personnel and our energy businesses due to lower activity levels. However, given overall lower volumes we reduced our workforce by a total of 1,111 during 2015 across several of our operations including our energy businesses. This was offset by increased headcount of 255 at certain of our businesses that were growing in 2015 mainly in our toll processing and aerospace locations. Company-wide, our net headcount at December 31 was down 5.8% or 856 employees compared to the beginning of the year on a 2.8% decline in tons sold.

Our strong gross profit margins including LIFO income and effective expense control resulted in the 2015 full-year non-GAAP operating income margin of 6.4%, an improvement from 6.1% in 2014. Our effective income tax rate for the 2015 fourth-quarter was 27.1% compared to 26.6% in the 2014 fourth quarter and 32.1% in the 2015 third quarter. The variances are mainly due to timing of recording certainly quarterly adjustments. For the full years of both 2015 and 2014, our effective tax rate was 31.1%. We currently expect that our full-year 2016 effective income tax rate will be approximately 31.5%.

Our Non-GAAP net income attributable to Reliance for the 2015 fourth-quarter was $63.3 million or $0.87 per diluted share compared to $79.1 million or $1.01 per diluted share in the 2014 fourth quarter and $85.8 million or $1.16 per diluted share in the third quarter of 2015. Our earnings release issued earlier today includes a reconciliation of our non-GAAP adjustments.

We generated $308.7 million of cash from operations during the 2015 fourth-quarter resulting in a record $1 billion for the full year of 2015. This reflects the strong execution of our team, increasing gross profit margins in a declining price and volume environment along with our focus on inventory reductions and demonstrates the countercyclical nature of our working capital needs. On the working capital front, we continue to manage our receivables well with their accounts receivable days outstanding rate at December 31, 2015 of 42.4 days in line with our historical range. Our inventory turn rate at December 31 was 3.9 times based on dollars and 4.5 times or 2.7 months on hand, based on tons which improved from our 2014 rate of 4.4 times based on tons.

We used our strong cash flow from operations to reduce our debt balance, grow our existing businesses, and return value to our shareholders. We paid down $167.5 million of debt during the fourth quarter for a total of $376.6 million for the year. At December 31, 2015, our total debt outstanding was $1.9 billion resulting in an improved net debt to total capital ratio of 31.8% and net debt to EBITDA of 2.25 times. As of December 31, 2015 we had $332 million outstanding on our $1.5 billion revolving credit facility. We funded our purchase of Tubular Steel in early 2016 with borrowings on our credit facility resulting in a pro forma net debt to total capital ratio of 35.1% and leaving significant liquidity with over $800 million still available for borrowings after funding the acquisition. We spent $172.2 million on capital expenditures during 2015. Looking ahead to 2016 we expect to spend approximately $180 million on capital expenditures a majority of which will be related to supporting organic growth initiatives including opening new facilities and increasing our value added processing capabilities.

We also paid quarterly dividends totaling $120.1 million in 2015 and further enhanced our shareholder returns with opportunistic share repurchases. In 2015, we repurchased $355.5 million or 6.2 million shares of our common stock at an average price of $57.39 per share. As a result of these repurchases, we realized an earnings per share benefit of $0.19 per share in 2015. On a pro forma basis, that is if we would have repurchased all of the 6.2 million shares on January 1, the impact on earnings-per-share would have been $0.34 for the year.

As a reminder, because of our significant share repurchase activity in 2015 our Board of Directors amended our share repurchase program increasing by 7.5 million shares the total authorized number of shares available to be repurchased and extending the plan through December 31, 2018. The 8.4 million remaining shares authorized for repurchase represent approximately 12% of our current shares outstanding. We expect to use our available cash to continue reducing our outstanding debt balance, supporting our various growth initiatives, paying a quarterly dividend, and opportunistically repurchasing shares of our common stock.

Now, turning to our outlook we are confident in our ability to execute well in the current environment. As we're optimistic that the US economy will continue it's slow growth going forward. As a result, we estimate a sequential increase in tons sold of approximately 6% to 8% in the first quarter of 2016 over the fourth quarter of 2015 which includes the normal seasonal increase in shipping volumes compared to the fourth quarter as well as additional volume from our purchase of Tubular Steel. We believe that metals pricing for most products we sell has stabilized at the current low levels with the potential to improve slightly in the first quarter as a result of the price increases announced for a number of the products the Company sells. Accordingly, we expect our average selling price in the first quarter of 2016 to be flat to up 1.5% from the fourth quarter of 2015. Given this pricing scenario as I mentioned earlier we do not anticipate a LIFO adjustment in the first quarter of 2016. As a result, we currently expect non-GAAP earnings per diluted share to be in the range of $0.80 to $0.90 of the quarter ending March 31, 2016 compared to non-GAAP earnings per diluted share of $0.87 in the fourth quarter of 2015 which included net LIFO income of $42 million or $0.35 per share.

In closing, we would like to once again thank our managers in the field for their exceptional execution in 2015. We remain confident in our ability to continue to effectively manage the controllable aspects of our business, to mitigate the volatile factors that continue to impact our industry. Our record cash flow in 2015 was a direct result of our increased gross profit margins along with effective working capital management including our inventory reduction initiatives. Our strong cash generation allows us to continue to fund growth opportunities while at the same time providing steady returns to our valued shareholders.

That concludes our prepared remarks. Thank you for your attention, and at this time, we would like to open the call to questions. Operator?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Timna Tanners, Bank of America, Merrill Lynch.

Timna Tanners - *BofA Merrill Lynch - Analyst*

Hello, good morning. Okay guys. I wanted to just ask you for a little bit more refinement on the volume guidance, because, on the one hand you say Q4 was particularly -- a little disappointing on volume. And then, we have heard that our [channel tecs] say January is a pretty strong month, so 6% to 8% would compare with your historical 9% and [MSCI] at like 9.6%, and as you point out, you tend to beat the MSCI. Just wonder if you could tell us why you think the sequential improvement might be less than it has been in recent years.

Gregg Mollins - *Reliance Steel & Aluminum Company - President & CEO*

I'm not sure that it's going to be sequentially different than years past, if we have 9% -- I'm not sure we have done that every year over the past five years.

Timna Tanners - *BofA Merrill Lynch - Analyst*

Average capacity (inaudible).

Karla Lewis - *Reliance Steel & Aluminum Company - Senior EVP & CFO*

Yes, Timna we look at we are trending so for into 2016, and look at how January is kind of a light month. So we're using the visibility from what we've seen so far in January, which we think is healthy demand. We've seen it bounce back from where we were.

There is still the energy drag on tons, which is only a small portion of our business, but we may be a bit conservative, but we tried to make what we felt was a reasonable estimate. Looking at January and the MSCI data and their comparison to January of last year, we are certainly better with what we've seen in January than that. But we think the 6% to 8% is a good reasonable estimate that shows demand coming back the way we would expected it to.

Gregg Mollins - *Reliance Steel & Aluminum Company - President & CEO*

Really, where we see the turning point, Timna, is really in the month of March. January, February, is always a little bit soft in the first quarter. And March really is kind of indicative of what were going to see, basically, in the second quarter. So, I think we will always be a little bit conservative on our guidance in the first quarter. Based on what we're seeing in January and part way through February, with the telling point being really in the month of March.

Timna Tanners - *BofA Merrill Lynch - Analyst*

Okay. That makes a lot of sense. And then secondly, I wanted to ask about the Tubular Steel acquisition. It looks like, if we interpreted this correctly, with the revolver that's tapped about $370 million was the deal, correct me if I am wrong, and then revenues you said were $200 million. If you could talk about the rationale on that transaction, and if you think the $200 million is depressed on a normalized basis. It wasn't clear if it was -- how much of that was related to the energy markets, and not related to energy markets. So, a little more detail, if you could.

Karla Lewis - *Reliance Steel & Aluminum Company - Senior EVP & CFO*

Yes. So, Timna, just on the number you came up with, would not be the right number. We haven't disclosed our purchase price amount for the Tubular Steel acquisition, but it was in line with the way we've consistently valued companies over the years on a normalized pre-tax income basis; and Greg or Jim can talk a little more about Tubular. But with the markets they are in, the $200 million is their 2014 revenue. They do have some energy exposure, so their numbers are down a bit currently from that 2014 amount.

Gregg Mollins - *Reliance Steel & Aluminum Company - President & CEO*

Yes, they're 2014 numbers, Timna, at roughly $200 million in revenue; in 2015 it was less than that. In good times, in the energy business, the percentage of their revenues are about 35% to 40%, related to energy. In these times, it's roughly 25% to 30%. They sell quite a bit of their metal into the energy market through service centers, as well. So we've included that in those percentages.

Jim Hoffman - *Reliance Steel & Aluminum Company - EVP, Operations*

Hi Timna, this is Jim. TS, it's just a fine Company. They do have energy exposure, but they also sell into a lot of other markets that we anticipate to do quite well. They are well-run Company, been around for a long time. They have a great name in the marketplace, and they fit in very well with us.

Gregg Mollins - *Reliance Steel & Aluminum Company - President & CEO*

They have a lot of products, Timna, that are very special to themselves. The inventory turn isn't what our inventory turn is, because of these specialized products. We expect that we can help improve that, but I don't think it will ever be at the levels of which we are at, because of the specialty nature of the products that they have.

But we've been admiring them from afar for many, many years now, and we are very, very pleased that they are now part of the family.

Karla Lewis - *Reliance Steel & Aluminum Company - Senior EVP & CFO*

And similar to the other Reliance Companies with the specialty items, where their returns are typically a little lower than the Company-wide average, they also typically have higher than average gross profit margins which Tubular Steel certainly has.

Timna Tanners - *BofA Merrill Lynch - Analyst*

Okay, thanks for all that.

Operator

Phil Gibbs, KeyBanc Capital Markets.

Phil Gibbs - *KeyBanc Capital Markets - Analyst*

Good morning, thanks very much.

Gregg Mollins - *Reliance Steel & Aluminum Company - President & CEO*

Good morning, Phil.

Phil Gibbs - *KeyBanc Capital Markets - Analyst*

I had a question on what your expectations are for the toll processing business in 2016, 2017. Obviously, a lot of invests you've made, any way to couch how much either incremental volume or incremental revenue you expect? Anything that could help us frame that out.

Gregg Mollins - *Reliance Steel & Aluminum Company - President & CEO*

We have made, Phil, as you know, some pretty sizable investments, both last year, and this year going forward. Primarily to support the exposed aluminum going into the automotive and truck business. To what extent their revenue growth is going to be -- you know, when you look at the overall Company revenue compared to what we are bringing in toll processing, it's a very small portion of our overall revenue. It's a larger portion of our overall profitability. But you know, it's hard -- Karla, do you have any comments about the revenue increase?

Karla Lewis - *Reliance Steel & Aluminum Company - Senior EVP & CFO*

Yes, it was about 3% of our revenue in 2015. It's hard to move that a lot, because of the nature of their business, where we're just charging processing fees. As Jim stated in his comments, we basically doubled their aluminum processing in 2015 over 2014 levels.

We expect to continue to increase that because the one facility that did a lot of the new processing of aluminum didn't get started up until, really, I think about April of 2015. So we will have a full year with that. And we did make more investments, and are continuing to make investments, so we would certainly expect continued aluminum growth, tolling growth there. But could it get to 4% of revenue? Possibly, but it takes a lot to move that percentage.

Gregg Mollins - *Reliance Steel & Aluminum Company - President & CEO*

Just by way of volumes though, Phil, as Jim pointed out, we doubled our aluminum pounds out the door starting up with that new facility in April, so really, we had an eight month run. We are adding another piece of equipment there, that should be operational towards the end of the second quarter?

Jim Hoffman - *Reliance Steel & Aluminum Company - EVP, Operations*

Right.

Gregg Mollins - *Reliance Steel & Aluminum Company - President & CEO*

Okay. So we would expect that our increase in volumes in aluminum would be about 50% higher in 2016 over 2015. Okay? But as we pointed out before, there's no metal that we're charging for, so the actual dollars, you know, going into revenue are quite misleading.

Karla Lewis - *Reliance Steel & Aluminum Company - Senior EVP & CFO*

And they also -- with our tolling businesses, even though the revenue dollars are light because of that, the volume that they process is significant. Once again, in 2015, our toll processing operations processed more metal then the rest of the Company sold on a combined basis, so if they were buying and reselling the metal, we think the tolling businesses would be at least an $8 billion-plus revenue.

Jim Hoffman - *Reliance Steel & Aluminum Company - EVP, Operations*

Hi Phil, this is Jim, as well know (multiple speakers), they are not only an aluminum processor. They process a lot of steel that goes into refrigerators, dryers, all that appliance-type business, too. And that's a robust business, and that continues to do well as we go.

Phil Gibbs - *KeyBanc Capital Markets - Analyst*

Okay, thanks for that color. And, Karla, what were your gross margin assumptions for Q1, in terms of how we should be thinking about that FIFO-wise?

Karla Lewis - *Reliance Steel & Aluminum Company - Senior EVP & CFO*

Yes, so we didn't actually give those. We'd said that we expect to continue to execute well, and we think executing well is -- reflects strong FIFO gross profit margin. So, we don't see any direct reason for our gross profit margin to change significantly on a FIFO basis, from where we've been running towards the end of the year.

Phil Gibbs - *KeyBanc Capital Markets - Analyst*

Okay. And then, lastly, I know you had mentioned in your prepared remarks -- I think you said a $69.1 million lower cost or market. How common is that, and can you give us any color as to how that flowed through the year? Because I think right now, you said that the reserve went to a debit position, so just any color that you can provide us on the timing and the flow-through, that would be helpful. Thank you.

Karla Lewis - *Reliance Steel & Aluminum Company - Senior EVP & CFO*

Yes, Phil. So, it's not that common to end up in a debit LIFO reserve, but as you guys have all been writing about, prices are at levels not seen for many, many years. And, so that caused, with the significant mill price reductions this year, that generated a lot of LIFO income. In the third quarter, we started to look at that. Typically your LIFO reserve is a credit, and generally provides some cushion where you don't necessarily typically record lower of cost or market reserves, because it kind of lowers your inventory costs on hand.

When you flip to a debit LIFO reserve position, which we did with $186 million worth of LIFO income in the year, that actually makes your inventory cost higher by that debit LIFO reserve. So, actually, in the third quarter we started booking to a lower of cost or market reserve just because current replacement costs were lower than our inventory costs on hand. So, it was about $69 million. We ended up with a net reserve between LIFO and LCM of a $26 million credit. We think that's a pretty low number, even the $69 million lower of cost or market reserve is not that much when you look at $1.4 billion of inventory on hand.

Phil Gibbs - *KeyBanc Capital Markets - Analyst*

I appreciate that. I just was curious, given that I never heard you talk about that before.

Karla Lewis - *Reliance Steel & Aluminum Company - Senior EVP & CFO*

Yes, it's the first time we've had it, actually. I think back in 2002, we were close with some of the lower prices then. And you will see it more commonly for companies that are on FIFO instead of LIFO. Because when you are on FIFO they have to measure it more frequently. They don't have that kind of cushion in their LIFO reserve that I mentioned.

Phil Gibbs - *KeyBanc Capital Markets - Analyst*

Okay. Thanks so much.

Operator

Michael Gambardella, JPMorgan.

Michael Gambardella - *JPMorgan - Analyst*

Yes, good morning (multiple speakers). A couple questions: on aluminum, where you're seeing a lot of import pressure, from what country or countries, and what products, if you could give us some color on that?

Bill Sales - *Reliance Steel & Aluminum Company - EVP, Operations*

Most of the pressure -- if you are referring to heat-treat products and general engineering, a lot of it's coming from Asia. Coming out of China, there's several new mills there. But it comes from, really, all over the world. There will be some coming in from South Africa, so there's a -- on the general engineering side, there's a lot of import availability. Now, on the aerospace side, many of those mills are not qualified or certified to produce aerospace products, so you don't get that same pressure on the aerospace side.

Gregg Mollins - *Reliance Steel & Aluminum Company - President & CEO*

Common alloy.

Bill Sales - *Reliance Steel & Aluminum Company - EVP, Operations*

Common alloy that is -- there's a lot of import product. And that, again, coming out of Asia, some coming in from Europe, and in that market where a lot of the domestics have been focused more in the opportunities on the auto side, there is a lot more import coming in and being used for distributor coil.

Michael Gambardella - *JPMorgan - Analyst*

And have you taken advantage of these low price imports, or are you seeing some of your competitors taking advantage of it?

Bill Sales - *Reliance Steel & Aluminum Company - EVP, Operations*

We do, on common alloy it's pretty common, I think as the industry -- because of the more focus on the auto from the domestic mills. The common alloy product is -- a big part of that is import product, and I think both with us and our competitors. On the general engineering side, so far we're still predominantly on the domestic part of that, and we will participate to a smaller extent with import product.

Michael Gambardella - *JPMorgan - Analyst*

Okay. And, just in terms of the guidance on the volumes up 6% to 8%, just a follow-up question on that. Assuming you back out the seasonality and the acquisition of Tubular's, what would that number be?

Karla Lewis - *Reliance Steel & Aluminum Company - Senior EVP & CFO*

Yes. You know, that's kind of hard to answer, Michael, because we're so used to the seasonality. It's always the fourth quarter to first quarter experience that we see. One of the things that does change at Reliance as we acquire companies, is some of the Companies traditionally have the second quarter as their strongest volume quarter, but some of the Companies typically have first quarter as their strongest. So that mix is where acquiring Companies can shift those seasonal patterns a bit. I would say we're up marginally, if you backed out seasonality, it's just really hard for us to think about backing out seasonality.

Michael Gambardella - *JPMorgan - Analyst*

Right, so, but backing out seasonality in the acquisition, you feel your volumes would still be up a little bit, quarter to quarter?

Karla Lewis - *Reliance Steel & Aluminum Company - Senior EVP & CFO*

Yes, we think they would still be up a bit quarter over quarter, yes.

Michael Gambardella - *JPMorgan - Analyst*

Great, thank you.

Operator

Aldo Mazzaferro, Macquarie.

Aldo Mazzaferro - *Macquarie Research - Analyst*

Hi, good morning, everyone (multiple speakers). So, Greg, on the overall market outlook, when you look at the service centers, I noticed Karla mentioned we haven't seen an inventory debit or close to it since 2002. If you look at the market today, and you say we are in this market that might be similar to that period of time where, maybe, the 2000 market -- do you see your -- you are in a position where you have cash, you have a strong balance sheet, where a lot of other service centers have either little cash, or low valuations, or both, and weak balance sheets. I'm wondering if you see the pace of acquisitions picking up in 2016?

Gregg Mollins - *Reliance Steel & Aluminum Company - President & CEO*

I think that -- here's just one opinion, right? There's four of us sitting in the room, so you'll probably get four different opinions, if you want to know the truth, but the fact of the matter is 2015 was challenging, with the prices going down basically 15 months in a row, starting in September of 2014, and each and every month going forward, on basically every product that we stock. When you are going through a period of time like that, companies aren't doing as well, financially, and they are not as willing to shop their company in the marketplace, and sell their company. They think the values are going to be undervalued for the reasons I just explained.

So, with stability, unfortunately at a very low level, okay, but we believe that hopefully we'll get a little bit of upswing going forward in the year. When prices are more stable, profitability is a little bit better, and the likelihood of them wanting to go out and maybe shop their company if there's an interest is a lot better than in a declining pricing environment. So, that's a long-winded version of me saying I think, yes, 2016 will probably -- there will be more activity than 2015. But we're going to have to look at the deals on an item-by-item basis, and make our own decision on whether or not we going to go forward.

We were very fortunate with the Tubular Steel. It wasn't shopped, they came to us, basically exclusively. And with their specialized products and whatnot, it was a very attractive acquisition for us. I think there's going to be more activity, I think we are already seeing that. Looking at deals, whether or not we'll get them done, or want to get them done, that always remains to be seen.

Karla Lewis - *Reliance Steel & Aluminum Company - Senior EVP & CFO*

Yes, I think also, Aldo, to your point of us having a strong balance sheet, and we will continue, as Greg said, to look and execute on the right acquisition opportunities. But we also are continuing to invest a lot in our existing Company, and a lot of our competitors out there don't have the ability to do that. So, we expect to continue to pick up market share because of our ability to finance -- we have the funds available to capitalize on opportunities that we see out there in the market. And so, you see a strong CapEx budget for us again this year, as we've had last few years, because we'll continue our growth that way, and are fortunate to that the balance sheet that we do to be able to do that.

Aldo Mazzaferro - *Macquarie Research - Analyst*

Karla, if I could follow up on a separate topic. In terms of your gross margins on a FIFO basis, if you look at the fourth quarter, I'm sure there was some penalty on those margins from the fact of pricing on the sale point was lower than it was on the purchase point. I think you probably felt that kind of pressure throughout the year. Do you see, for example, if the prices were to stabilize in first quarter, stay there for 60 days or longer, do you see some margin pressure being relieved? And maybe you could say how many basis points you think your penalty was in the quarter?

Karla Lewis - *Reliance Steel & Aluminum Company - Senior EVP & CFO*

Yes so, Aldo, generally we do expect that if prices are stable or up slightly, we do expect to be able to expand our gross profit margins in those types of environments. That being said, we are at a good healthy rate, the way we ended the year. We're not brave enough I don't think to sit here and try to quantify what that number would be, but you are correct that with the really strong execution we had of reducing inventory during the year while prices were going down. We do think we are in good position now with our inventory costs that we have on hand to support strong gross profit margins going forward.

Gregg Mollins - *Reliance Steel & Aluminum Company - President & CEO*

Yes, Aldo, we were extremely proud of many aspects of our business, but in particular our gross profit management and our inventory reduction were the two highest on the list. Generally speaking, when you have a declining market in prices like we had 15 months in a row, it's very unusual for you to get your margin expansion. Especially when you do it four quarters in a row, so -- but we were reducing our inventory substantially throughout those quarters, so, in large part, we were able to -- when you had too high of inventory, [you're] able to chase bad orders, okay, because you have to reduce those inventories.

Our inventories were in line, I think we got a head start on it. We started looking at our inventories very closely in the fourth quarter of 2014, okay, because that's when the mills started to reduce their prices with September of 2014. So, we were pleased with that. But now, with the prices more in line and more stable than they have been for almost a year-and-a-half, I think we would expect maybe a little bit of improvement on the margin side.

Aldo Mazzaferro - *Macquarie Research - Analyst*

Well thanks, Greg. Congratulations on the excellent performance in a tough market.

Gregg Mollins - *Reliance Steel & Aluminum Company - President & CEO*

Thanks, Aldo.

Operator

(Operator Instructions)

Chris Olin, Rosenblatt Securities.

Chris Olin - *Cleveland Research Company - Analyst*

Hi, thanks for taking my call.

Gregg Mollins - *Reliance Steel & Aluminum Company - President & CEO*

Good morning, Chris.

Chris Olin - *Cleveland Research Company - Analyst*

I just had a quick question on aerospace. Seems like there's a bit of discussion about a potential inventory glut within the channel. Perhaps some of this relates to the recent production cuts at Boeing in some of the wide-body aircraft. I guess I just wondering if you saw this impacting your business right now, and is that reflected in the volume guidance as well?

Bill Sales - *Reliance Steel & Aluminum Company - EVP, Operations*

Hi Chris, it's Bill Sales. You know, there has been a lot of discussion and a lot of articles about that. From our point of view, we really look at where mill lead times are, where the build rates will follow that, and we'll look at the backlog. And, while there have been some adjustments in the build rate, I think there is -- a lot of that is tied to conversions to the next-generation aircraft. I know in one case it's really tied to the lack of freighter activity. But we really see strong demand, mill lead times are 25-plus weeks. And we think that demand will continue through this year. And we feel good about the programs that we are on, we feel good about our position with opening some new facilities. So, we really think that 2016 is going to be another very, very strong year for us in aerospace.

Chris Olin - *Cleveland Research Company - Analyst*

Great. Just back to the lead time issue. Are you having any trouble getting some of the materials, and I've heard some backing up on the titanium side. Is there any problem in terms of the supply?

Bill Sales - *Reliance Steel & Aluminum Company - EVP, Operations*

Not for us. I think we've got good relationships there, and programs in place, so the supply side isn't a problem for us. You do have to have programs to work through some of these long lead times that we are dealing with, and if the question isn't about titanium specifically, I think we are in really good shape there. With our mill relations -- and that market, we're not -- from a lead time standpoint, you do need some programs in place to be sure you can get the product when you need it.

Chris Olin - *Cleveland Research Company - Analyst*

Thanks a lot.

Operator

Thank you. We've reached the end of our question-and-answer session. I will turn the floor back over to Mr. Gregg Mollins with any closing remarks.

Gregg Mollins - *Reliance Steel & Aluminum Company - President & CEO*

Well, listen, thanks again for your support and for participating in today's call. And we would like to remind everyone that in March we will be in New York City, presenting at Macquarie's What's Next for the Non-Res conference, so we hope to see many of you there. And have a great day. Thank you.

Operator

This concludes today's conference. Thank you for your participation. You may now disconnect your lines at this time.