
MANAGEMENT DISCUSSION SECTION

Operator: Welcome to Thermadyne Holdings Corporation First Quarter Financial Results Conference Call. At this time, all participants are in a listen-only mode. After the presentation, we will conduct a question-and-answer session. [Operator Instructions]. This call is being recorded. If you have any objections, you may disconnect at this time.

Now, I would like to turn the meeting over to Chairman and CEO, Paul Melnuk; and CFO, Steve Schumm. You may begin.

Paul D. Melnuk, Chairman, Chief Executive Officer and President

Thanks, Kelly . Good morning, everybody, and I would also like to welcome you to this first quarter earnings conference call. As Kelly indicated, my name is Paul Melnuk, Chairman and Chief Executive Officer; and with me today is Steve Schumm, our Chief Financial Officer.

We issued a press release over the weekend with our 2009 first quarter results, and we also filed a Form 10-Q with the SEC. A copy of the press release and 10-Q filing may be obtained from our website at www.thermadyne.com or by contacting Investor Relations at 636-728-3031.

As we begin, let me remind you that this call may contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These statements reflect management's current expectations and involve a number of risks and uncertainties. Actual results may differ materially from such statements due to a variety of factors that could adversely affect the company's operating results. These risks and other risks relating to our business are set forth in documents filed with the Securities and Exchange Commission, specifically our most recent annual report on Form 10-K, and other reports filed from time to time with the SEC.

In a moment, Steve will discuss in detail the 2009 first-quarter financial results. Before he does, however, let me offer a few highlights.

Over the past few years, we have made substantial improvements to our business. We have been aggressive operationally, taking significant costs out of the business, improving customer service, and developing a pipeline of new products. Financially, we have been prudent to reduce debt levels and extend maturities. As a result, we have been much better positioned to meet the challenges of the most difficult business environment that we have faced in our lifetimes.

Cash flow and liquidity are important measures of a company's health in difficult times such as we're experiencing today globally. At quarter-end, cash and available credit was \$30 million, which is ample for our business. We also generated cash flow from operations despite a very challenging operating environment. Importantly, we do not have any significant debt maturing for several years, while the prospects for improved cash flow, particularly in the back half of this year, are encouraging.

Despite the difficult first-quarter results, we are pleased with the progress we've been – that we have made resizing our business with the reality of much lower volume levels that the global recession has presented. We hope there will be a quick improvement in the global market. However, we do not manage our business on hope, rather we're managing on the basis that we must be able to generate sustainable returns at current sales levels. As a result, we've taken action on resizing while we continue to execute our business plan to improve operations and grow profitably with better customer service, effective new products, and selective market expansions while aggressively reducing cost of operations and the cost of making our products.

I'll have additional comments on our results and the outlook for the business once Steve has completed his review of the financial results for the quarter. Steve?

Steven A. Schumm, Chief Financial Officer, Chief Administrative Officer, Principal Accounting Officer and Executive Vice President

Thanks, Paul, and good morning. Net sales were 83.3 million in the first quarter of 2009, a decrease of 36% over the prior year. Our sales decreased 30% excluding the effect of foreign currency translations. The sales declines were generally comparable across all geographic regions. Our export sales to Latin America and the Middle East markets declined over 50%, our filler metal and hardfacing product lines declined approximately 20%, with the other product lines declining approximately 40%.

In the first quarter, our gross margin percentage was approximately 26%, as compared to approximately 32% in the prior year. The reduced gross margin in the first quarter reflects a six percentage point reduction due to charges of approximately \$5 million from operational inefficiencies arising from the low volumes.

Over the course of the first quarter, we continued and expanded the cost reduction programs that our operations team commenced late last year. We implemented layoffs and other cost reduction programs at all of our global locations in response to the precipitous decline in orders during the quarter and the increased need to reduce inventories. Our efforts reduced first-quarter labor and overhead expenses by more than 30% from the prior year and we reduced inventories by 13%. The impact of our efforts as the quarter evolved is evidenced through a closer look inside our first quarter numbers. While costs were down 30% for the quarter, our labor and overhead expenses in the month of March were down 40% from last year and 15% below the average for the first quarter.

In addition to these charges for manufacturing inefficiencies, we had charges of 1.7 million or two percentage points from higher cost raw materials committed to in 2008 that impacted the first quarter. As we look forward, this largely ends the net charges associated with high cost raw materials. With respect to the charges for manufacturing inefficiencies, we have recalled some of our production staff and our production is slowly ramping up. We estimate the charges for manufacturing inefficiencies will decline steadily over the remainder of the year. Accordingly, we anticipate that gross margins excluding LIFO effects will increase in the second quarter and more noticeably over the remainder of the year.

SG&A costs were 19.4 million in the first quarter of 2009. Excluding the special \$1.3 million severance charge recorded during the quarter, our SG&A expenses were 21.8% of sales compared to 21% in the prior year's first quarter. Overall, this is a good result given that many of the actions to reduce costs were not in place until the end of January.

We recorded the severance charge accrual for amounts payable to employees who have elected to participate in a voluntary retirement program. The severance amounts will largely be paid over the next six months. The voluntary early retirements are estimated to provide annual savings of 2.6 million. We believe we will be able to maintain SG&A expenses as a percentage of sales at these levels over the rest of the year.

Interest cost declined \$700,000 in the first quarter to 4.6 million as compared to the first quarter of 2008. Our debt balances averaged \$225 million in the first quarters of both 2009 and 2008. Our average effective interest rate of 8.3% in the first quarter of 2009 was 120 basis points less than in the prior year due to declines in LIBOR and in the special interest adjustment on our bonds.

As we look forward, the special interest adjustment on the bonds increases 50 basis points effective April 1, and another 50 basis points on July 1, 2009 because of our increased leverage ratio. We do not foresee the special interest adjustment going any higher than that in 2009.

With respect to EBITDA, a schedule is attached to the earnings release showing the detailed computation for the quarter. Adjusted operating EBITDA from continuing operations was 3.6 million or 4% of sales in the first quarter of 2009 as compared to 17.7 million, almost 14% of sales, in last year's first quarter. As we look to the second quarter and beyond, we estimate EBITDA will be increasing significantly as we now start realizing more normalized gross margin profitability as noted in my previous remarks.

Let's now take a closer look at our cash flows. During this first quarter, we generated \$3 million in cash flow from operating activities. This approximated the 2.9 million generated last year in the first quarter. This cash flow from operating activities will noticeably increase as we progress throughout the year toward the estimated 20 to \$25 million of cash flows previously forecasted for the year, as a result of improving earnings and further working capital reductions.

During the first quarter, this net \$3 million of cash flow from operating activities included \$23 million of cash generated from accounts receivable collections and inventory reductions. However, approximately \$8 million were used to reduce our trade payables position. Our supplier financing represented only 25% of inventories at March 31, 2009 versus 40% last March, and 30% at December 2008. As we look forward, our large net investment in inventories will serve as a source of cash flow.

As is typical in our first quarter, we used almost \$16 million of cash in payment of our semi-annual interest payments and amounts payable for customer rebates, incentive compensation, and severance payments. In the first quarter of 2009, we also used 2.2 million of cash to acquire manufacturing equipment that was ordered during 2008, and we expect a comparable amount of equipment deliveries in the second quarter.

As of March 31, 2009, we had \$30 million of cash in unused availability through our working capital facility with GE. This represents a low watermark in this measure of liquidity and we see it increasing steadily from here. With respect to our overall debt arrangements, as we've discussed in the past, our only significant covenant under our agreements is the fixed charge coverage test under the working capital facility with GE. Fixed charges include unfinanced equipment purchases, and as a result, we are in discussions to arrange equipment financing to build the cushion under this covenant.

With that, I'll turn it back to Paul.

Paul D. Melnuk, Chairman, Chief Executive Officer and President

Thanks, Steve. The first quarter was difficult; however, we like others are encouraged by the apparent stabilization of end markets during the quarter, albeit at levels substantially lower than prior years. While we are confident about the long-term growth prospects of our end markets, it is difficult to predict when our markets will transition from this period of stabilization to a period of strong growth like that which was experienced prior to the economic downturn.

In the meantime, we are intentionally focused on resizing the business and improving our performance for the long-term. In this regard, we are pleased with the overall progress we've made to position us to generate attractive sustainable returns at current sales levels. And the real positive of this is that we have ample opportunity for additional savings in product and operating costs from where we are today.

In terms of specific actions, we reduced variable costs as much, and in many cases, more than the decline in volume in the quarter. With fixed costs, we took action to resize our selling, general, and administrative costs such these were essentially the same percentage of sales this year as they were in 2008. Good progress was also made taking fixed costs out of the manufacturing operations, although it is difficult to align these costs with lower sales volumes in a short period of time. We are, however, aggressively working to restructure our operations to resize the fixed costs as quickly as possible.

Finally, we aligned the supply chain with the reduced volume. As a consequence, production levels were much lower than sales levels in the quarter, which adversely affected fixed costs absorption. However, inventories were reduced by \$13 million, contributing to the positive operating cash flow in the quarter.

These necessary actions adversely impacted reported results in the quarter, but position us for improved performance over the remainder of the year. In particular, production volume should increase to more closely match sales levels, which will improve fixed costs absorption and other operating efficiencies as well as producing more savings from our TCP continuous improvement process. Other costs will also decline.

Beyond this, we have a great deal of focus on reducing product costs through value engineering efforts. Our people are generating lots of opportunities that are being carefully considered with plans being developed to implement many of them. In addition, we are identifying opportunities to move component and finished goods manufacturing and sourcing to the best total cost location.

A highly attractive feature of our business model is the ability to quickly reduce our invested capital as sales volumes decline. To illustrate, we've reduced working capital nearly \$30 million over the last six months and expect it to continue to decline over the remainder of the year, providing additional cash flow. Further inventory reductions combined with the benefit of increasing accounts payable from higher purchases and production volumes are the main drivers of this benefit.

We are also pleased with the progress made servicing our customers. Delivery performance was excellent in the quarter and some new products were very successfully launched into the market. We also have additional new products to launch later this year that have generated very positive interest from customers.

We all know these are challenging times. However, we have a solid foundation built on a very attractive business model, strong brands, increasing cash flow, no significant debt maturities, and significant cost takeout opportunities. Although winded from the blow of the global recession, we are catching our breath and look forward to reporting much improved performance over the quarters to come.

And with that, Kelly, I'd now like to open up the call to questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from Jon Braatz from Kansas City Capital. Your line is open.

<Q – Jonathan Braatz>: Good morning, Paul. Good morning, Steve.

<A – Paul Melnuk>: Good morning.

<Q – Jonathan Braatz>: A couple of questions. Number one, Paul, you were talking about some of the opportunities that you see lying ahead in terms of capital spending and other opportunities. What – how constrained will you be this year in terms of looking at those opportunities and acting upon them, given the business conditions right now? Are some of these things just ultimately going to have to be put off, and how much – how aggressive can you be on taking advantage of those things?

<A – Paul Melnuk>: Well firstly, we have a lot of opportunity to take cost out of our operations and out of our products that do not require any capital spending.

<Q – Jonathan Braatz>: Okay.

<A – Paul Melnuk>: So there's ample opportunity and we're intensely focused on those, and frankly have been intensifying our focus.

Now, there is also a lot of opportunity that we have to invest in much more efficient machining capacity and capability that has very, very attractive paybacks, and that requires some capital. Our approach to capital spending this year is that we intend and are looking for sources of equipment financing, so that we can continue to make the investments without putting undo pressure on the fixed charge covenant ratio that Steve referred to. And we've made some progress, we've got lots of discussions underway and we believe that we will be able to continue to make highly attractive selective investments over the course of the year.

<Q – Jonathan Braatz>: Paul, when I visited your Denton facility, I think that's one of the things that the manager was discussing that there was – and I think Steve had mentioned to me, that there was some, potentially some things you wanted to do there in terms of machine and that there might be some equipment financing from the city or county or whatever. Anything of that at this point?

<A – Paul Melnuk>: Those are still discussions that are underway, one of the alternatives that are, or one of many alternatives that are being pursued. The other thing I should mention, Jon, is that in the first quarter we took delivery of more than \$2 million worth of equipment. We have more equipment coming in the second quarter that had been committed to previously. So all of that equipment is coming in and will be benefiting operations. And much of that capital, I'll point out, is also going into the Denton facility.

<Q – Jonathan Braatz>: Okay.

<A – Steven Schumm>: And Jon, I might just tack on that if you look back to last year's third and fourth quarter, we put a number of pieces of equipment in place that had the follow on that Paul mentioned and oddly enough, or maybe it's obvious, is that in slower times like this when you put all the pain aside, it creates an opportunity to maybe accelerate something. So, some of our discussion is we were hopeful of trying to accelerate some of the concepts that the manager in Denton was talking to you, and we're still – hopefully we can get that done, but we do have to make sure we get the financing locked up and...

<Q – Jonathan Braatz>: Sure.

<A – Steven Schumm>: ...we got a number of things that are in the middle, that I think will get done, but it's little bit – a little slower than...

<Q – Jonathan Braatz>: Right.

<A – Steven Schumm>: ...we would like to.

<Q – Jonathan Braatz>: Okay. I didn't see much discussion in – I don't think I saw any of it, in terms of geographical performance. We're hearing things from other companies about China coming out of this recession faster or spending their stimulus money and so on and so forth. What can you tell us a little bit about sales performance by geography?

<A – Paul Melnuk>: The Americas markets and Europe are the weakest segments. We are seeing much better results out of Asia-Pacific, including for us an important market is South Pacific; Australia and New Zealand, has been performing better than Europe and the Americas. We're seeing, clearly seeing increased activity in China, and for us in China, we are selling a relatively limited product offering of our higher technology products and that – it's an important business and it is responding to the expanding economy there.

<Q – Jonathan Braatz>: Thank you very much.

<A – Paul Melnuk>: Thanks, Jon.

Operator: Our next question comes from Craig Carlozzi from Mast Capital. Your line is open.

<Q>: Yes, hi, good morning.

<A – Paul Melnuk>: Morning.

<Q>: Could you talk a little more about the flexibility of your new and reduced cost structure in an environment where topline is down another 10 or 15%? It sounds like you've identified a lot of stuff for the current run rate of sales, but I am wondering what that next level would look like.

<A – Paul Melnuk>: Well, I mean, we're frankly committed to continuing to resize our cost structure to align with sales volumes, and I think we've demonstrated that with – on the SG&A side, and we will continue to take the actions to keep those costs in line.

On the manufacturing side, the fixed costs embedded in the operations are more difficult to resize and align in a short period of time. But we are very aggressively looking at what needs to be done, can be done and will be done in our manufacturing operations to align the fixed costs.

So, it's just – for us, it's just part of another – just part of what we have to do. We're going at it aggressively. It takes some time and we're not looking to just get our fixed costs in that area down to where sales volumes are today, but rather to build in a cushion for any further deterioration.

<Q>: Right. Okay, so it sounds like you have identified what that next layer of cost reduction would be, if necessary.

<A – Paul Melnuk>: Yes, I'm – we're very pleased at the response that our entire organization has had to this. People are working together and there has just been a boatload of ideas and a willingness to look at things and to do things that, frankly in good times, unfortunately aren't quite as apparent.

<Q>: Yes. And last question. With respect to your new products, could you expand a little bit on what you have in the new product pipeline? I mean, should we think about these things as revolutionary, or are they simply slightly higher margin replacements of your existing older products?

<A – Paul Melnuk>: Well, our industry generally is relatively slow moving. We have had a lot of success. One example I'll give you is last year we launched a new low-cost welding machine into our South Pacific market with terrific success. We brought that – a similar product suited for the U.S. market into the U.S. and launched it late in the first quarter. It – our performance to date has like tripled what our forecasts were in terms of sales volumes for that product. It's a low cost, lightweight, good quality piece of equipment and is at a cost base, a price that gives us attractive margins.

We also have been doing some work in the gas equipment area in particular. The technology in that market segment is decades old. It's very, very old technology, proven technology. But we have – we have developed some very innovative features that – in both regulators and torches, regulators that we will be launching later this year, and we hope the torch will be able to follow it fairly closely behind.

So, those are some examples. It is true innovation and it's unique products that are providing better value to the customers. And that's why we're getting good response.

<Q>: Okay, thank you.

Operator: Our next question comes from Ross Haberman from Haberman Firm. Your line is open. Mr. Haberman, please check your mute button, your line is open.

Our next question comes from Reid Ellison from MD Witter Investments. Your line is open.

<Q – Reid Ellison>: Hi, good morning.

<A – Paul Melnuk>: Morning.

<Q – Reid Ellison>: Just looking a little bit at the inventory line, we're seeing that down maybe 10% from year-end and probably 17 off the third quarter peak. What do you guys think about the right level of that in relation to sales being down 30%?

<A – Paul Melnuk>: Well, I think the way to look at it is in terms of inventory turns. And at the end of the first quarter our inventory turns were about 2.8 times. Through the middle part of last year, in fact March of '08, I think our inventory turns were about 3.8 or 3.9 times. So, we are committed and are working towards getting ourselves back to a position where inventory turns are marching towards 4 turns and beyond. It takes some time to do that. We have to do it in a prudent and planned manner and – but there is, point of all of that is there is certainly ample room for more inventory takeout.

<Q – Reid Ellison>: Okay, perfect.

<A – Steven Schumm>: And I think we've got that – when we say we're going to ramp up production slowly and steadily, that's all part of the mix. Inventories continue to come down, but you start to get shortages in certain parts. So, you will see inventories continue to come down noticeably. Probably the only time that wouldn't be true is if we have the happy news that the economy reverses much faster than we're fearing it will.

<Q – Reid Ellison>: Okay, perfect. And then if we're looking at the supplier side, looking at your customers and destocking at your end markets, what are you – what are you guys seeing on that front?

<A – Paul Melnuk>: Well we've seen, as I mentioned, sales levels stabilize, and – which implies that the destocking is largely completed. Some of our larger national account customers that tend to carry more inventory in their system, there may be some continued destocking occurring there. But, we think it's largely behind us.

<Q – Reid Ellison>: Okay, perfect. And then turning a little bit to pricing and just hearing what the general chatter is out there, is – what's the situation on holding your last round of price increases and maybe talking to customers about, with the volumes down where it is, is there a lot of pushback on looking for discounts? What's the situation there?

<A – Paul Melnuk>: Well, price is an important consideration for our customers and what we are seeing is that the market, our market, generally has not been lowering prices. There's been a few small competitors that have lowered prices across the board. But the reality is that with long supply chains and just the nature of the supply chain, it's – a lot of that price deflation on material cost, takes a long time to work its way through the supply chain, and that is – that's continuing.

Our approach to pricing is to be competitive where we need to be with customers, to retain business and to selectively grow market share. But so far, I think one of the bright spots that we've had to date this year has been the success at managing that price volume relationship.

<Q – Reid Ellison>: And with the – your projections of flat gross margins through the end of the year, is that assuming flat pricing or is that assuming a certain level of giveback?

<A – Paul Melnuk>: Well to be clear, our remarks indicated that we expect gross margins to increase over the balance of the year. And that increase that we are anticipating does reflect erosion and discounting of price. Most of the increase in gross margin is coming from the fact that production levels will rise that will benefit our fixed cost absorption and benefit manufacturing efficiencies.

<Q – Reid Ellison>: Okay, perfect. Thank you.

Operator: [Operator Instructions] And we do have another question from David Escamilla from Global Platinum Securities. Your line is open.

<Q – David Escamilla>: Hi, so I was just curious in terms of whether or not you see the Chrysler bankruptcy and perhaps the upcoming GM one as a shock to sales. I know that on the BB&T Capital Markets presentation you gave, you had 35% of the end market as being transportation. I was just wondering if you could give a little more detail on that.

<A – Paul Melnuk>: Well, in terms of the end market, transportation, most of our products are used in connection with some of – in the automotive sector with some of the Tier 2 suppliers. The heavy part of the vehicle, the chassis system and frame in particular, within automotive assembly, generally it's a different type of welding than what we do. The bulk of the transportation sector that we benefit from is everything from railcars, truck transportation, and some heavy, heavier type of transportation. We think that that market, it appears like that market is stabilized along with many others, albeit at low levels. So, we really don't think that the bankruptcies will impact that business dramatically here in the short term.

<Q – David Escamilla>: Okay; that's very encouraging. Thank you.

Operator: There are no further questions at this time.

Paul D. Melnik, Chairman, Chief Executive Officer and President

Okay, thank you, Kelly and I'd like to thank everyone again for their time and participation in this call and I would just remind everybody that – about the solid foundation that we have here at Thermadyne. Our business model, our brands, increasing cash flow, no significant debt maturities and very significant cost takeout opportunities all give us optimism and confidence in the future improved performance of Thermadyne. Thanks and we look forward to reporting to you later this year.

Operator: Thank you for participating in today's conference call. You may disconnect at this time.

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