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MCFT - Q2 2018 MCBC Holdings Inc Earnings Call

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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Q2 Fiscal 2018 MCBC Holdings, Inc. Earnings Conference Call. (Operator Instructions) As a reminder, this conference call is being recorded. I would now like to introduce your host for today's conference, Chief Financial Officer, Mr. Tim Oxley. Mr. Oxley, you may begin.

Timothy M. Oxley - *MCBC Holdings, Inc. - VP, CFO, Treasurer & Secretary*

Thank you, operator, and welcome, everyone. Today's call is being webcast live and will also be archived on our website for future listening. Joining me on today's call is Terry McNew, MCBC Holdings' President and Chief Executive Officer. Our agenda includes a strategic overview by Terry, followed by my analysis of financials. Then, Terry will discuss our strategies for growth and expectations for the second half of fiscal 2018, followed by the Q&A session.

Before we begin, we'd like to remind participants that the information contained in this call is current only as of today, February 8, 2018. The company assumes no obligation to update any statements, including forward-looking statements. Statements that are not historical facts are forward-looking statements and subject to safe harbor disclaimer in today's press release.

Additionally on this conference call, we will discuss non-GAAP measures that may include or exclude special or items not indicative of our ongoing operations. For each non-GAAP measure, we also provide the most directly comparable GAAP measure. Our fiscal 2018 second quarter earnings release includes a reconciliation of these non-GAAP measures to our GAAP results.

Before turning the call over to Terry, I'd like to remind listeners that there's a slide deck summarizing our financial results in the Investors section of our website.

With that, I'll turn the call over to Terry.



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Terry D. McNew - *MCBC Holdings, Inc. - President, CEO & Director*

Thanks, Tim. I'd also like to thank everyone for joining us today. As you saw from today's press release, top line sales grew significantly in the second quarter, driven by double-digit gains on the Mastercraft side and the addition of NauticStar. As we further integrate NauticStar, we expect to realize additional efficiencies, which will favorably impact margins. Since acquiring NauticStar, we have made significant progress leveraging our industry-leading strengths and operational excellence and financial management to further improve NauticStar's output, quality and margin.

With more than 15 years of boat manufacturing experience, including a 200,000-square-foot manufacturing facility, NauticStar has a reputation for reliability, quality and consistency with a loyal network of dealers and customers, including professional and sport fishermen and recreational and pleasure boating enthusiasts. Throughout our business, we are continuing to see solid retail activity and are comfortable with current inventory levels as our dealer inventory turns are continuing to improve year-over-year. Moreover, we're diligently working with our strong dealer network to maximize their opportunities moving forward.

On the new product front, Mastercraft recently introduced the new XT25, our largest multi-purpose cross-over boat. Completing the XT series lineup as our fifth and largest addition, the XT25 welcomes a crew of up to 18 with a traditional bow and new interior layout, offering more rear facing seating than ever before, enhancing socialization and wake action spectating. The XT25's 2 new rear facing seat designs include a standard flip-up rear facing seat that can convert into a bench seat and an optional starboard pull-up rear facing seat with a raising backrest that also converts into a bench seat. Additionally, our new XStar began production in the second quarter. Dealer response has been unbelievably strong. Full sale orders are up nearly 400% from the exit rate of the previous XStar. We have ordered an additional set of tooling to meet the overwhelmingly strong demand.

Looking ahead to the second half of our fiscal year, we're optimistic about prospects with the sales and profit growth opportunities we have for both NauticStar and Mastercraft. Our shared commitment to operational excellence and innovation teamed with our strong diverse product portfolio position the company well for the remainder of fiscal 2018 and beyond.

Now I'd like to turn the call back over to Tim to go over our financials.

Timothy M. Oxley - *MCBC Holdings, Inc. - VP, CFO, Treasurer & Secretary*

Thanks, Terry. From a top line perspective, net sales for the second quarter rose \$27.3 million or 53.4% to \$78.4 million from \$51.1 million for the prior year period. The increase reflects the inclusion of NauticStar, which increased net sales by 39.5% or \$20.2 million. The remaining increase of 13.9% or \$7.1 million was attributable to an increase in Mastercraft unit sales volume, favorable product mix and price increases. Gross profit for the second quarter increased \$5.6 million or 39.5% to \$19.9 million versus \$14.3 million in the prior year period. The inclusion of NauticStar contributed \$3.5 million to gross profit. Growth in Mastercraft unit sales volume, a favorable product mix and price increases, offset by higher material and shipping costs, accounted for the remaining increase.

Gross margin decreased to 25.4% from 27.9% for the prior year period. This anticipated decrease was primarily due to the inclusion of NauticStar's gross margin, which is in the high teens versus Mastercraft's industry-leading high 20s margin.

On the expense front, selling and marketing expense rose \$1.3 million to \$3.7 million for the second quarter compared to year-earlier quarter, primarily due to the inclusion of NauticStar, which increased selling and marketing expense by \$0.6 million, a rise in dealer meeting costs and an increase in promotional activities related to the introduction of the redesigned 2018 Mastercraft XStar.

General, administrative expense totaled \$5 million versus \$4.8 million for through the prior year period. This increase stemmed mainly from a rise in advisory fees related to NauticStar acquisition and the inclusion of NauticStar partially offset by a decrease in litigation cost.

Turning to the bottom line. Fiscal second quarter net income totaled \$8 million versus \$4 million in the year-earlier quarter, driven by the inclusion of NauticStar and reduced tax rates from the enactment of tax reform. Adjusted net income was \$7.8 million or \$0.42 per share on a pro forma, fully diluted weighted average share count of 18.8 million shares. This compares with adjusted net income of \$4.9 million or \$0.26 per share in the



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prior year period. Adjusted net income for the second quarter was computed using a blended annual tax rate of 29% due to reform. Our annual effective tax rate is expected to be lowered to about 24% for fiscal 2019.

EBITDA was \$12.3 million compared to \$7.9 million in the prior year period. Adjusted EBITDA margin was 17.4% from 17.6% in the prior year period. Adjusted EBITDA was \$13.6 million, a 51.5% increase from \$9 million in the prior year period. See the non-GAAP measures section included in today's press release for a reconciliation of adjusted EBITDA, adjusted EBITDA margin and adjusted net income to the most directly comparable financial measures presented in accordance with GAAP.

In the interest of time, I won't discuss the details of our 6 months results today, but I will echo Terry's comments and reiterate that we are very pleased with our performance and look forward to the second half of fiscal 2018. I'll be happy to answer any year-to-date questions during the Q&A.

With that, I'd like to turn it back over to Terry for our outlook.

Terry D. McNew - MCBC Holdings, Inc. - President, CEO & Director

Thanks, Tim. Given our strong second quarter performance, we are very optimistic about prospects going forward, and we remain committed to our five-pronged growth strategies: developing new and innovative products, further penetrating the entry-level and mid-line segment of the performance sport boat category, capturing share from adjacent boating categories, strengthening our dealer network, and driving margin expansion through continuous operational excellence. For full fiscal year 2018 guidance, we continue to expect net sales growth to be in the high 30% range, including 9 months of NauticStar's projected net sales. Both Mastercraft and NauticStar's top lines are growing in the high single- to low double-digit range compared to the prior year. We expect to see adjusted EBITDA margins for Mastercraft, excluding NauticStar, to grow to mid-19% range from 19% in 2017. After taking the dilutive effect of the NauticStar acquisition, consolidated EBITDA margins are expected to be in the high 17% range. Adjusted EPS is expected to grow in the low to mid-40% range. NauticStar is expected to provide accretion of between \$0.15 to \$0.20 per share during the 9 months post acquisition.

For the fiscal 2018 third quarter, we expect net sales growth in the low 50% range and adjusted EBITDA margin to be above 17%. Adjusted EPS is expected to grow in the low to mid-60% range.

Now I'd like to turn it over to the operator for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question comes from Eric Wold with B. Riley FBR.

Eric Christian Wold - B. Riley FBR, Inc., Research Division - Senior Equity Analyst

A couple questions if I may. I guess, first of all, can you give us a sense of just any general trend you're seeing from consumers at the various boat shows that have taken place so far, I guess, especially in terms of their willingness to kind of move up in ASP?

Terry D. McNew - MCBC Holdings, Inc. - President, CEO & Director

Yes. It's actually, Eric, sales are strong at every boat show today. We measure boat shows every year with a 2-week follow-up per leads, and our boat show results with shows that have completed with 2 weeks of follow-up are up 20% over last year and that last year's boat show results were a record for us. And additionally, dealers were reporting more floor traffic and strong quality buyers. In one report that we saw just this week, our

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many customers were beginning the trade-in cycle. An example, we're seeing a lot of buyers with 5- to 10-year-old product that are now shopping again. So we're very optimistic. Our portfolio is as strong as it's ever been, and our transaction costs or our promotional activities in Q2 were pretty light, actually. And Tim, can get into that a little bit. So we're very, very positive to see a lot of higher-quality buyers at the boat shows. Keep in mind that tax reform not only is very favorable for Mastercraft but also for many of our consumers. So I think that's one of the things driving the demand we're seeing in boat shows.

Eric Christian Wold - *B. Riley FBR, Inc., Research Division - Senior Equity Analyst*

Okay. So make sure I understood that. On the tax rate, so the 24% tax rate, that's for fiscal '19 as well for the remaining 2 quarters of this year?

Timothy M. Oxley - *MCBC Holdings, Inc. - VP, CFO, Treasurer & Secretary*

No. We're going to have a 29% rate. That's our blended rate for fiscal '18. So we're going to reflect that in each quarter. And then in fiscal '19, the full effect of the tax change, which occurred midyear for us, will be in effect. So that's going to have a blended rate of 24%, which includes state, correct.

Eric Christian Wold - *B. Riley FBR, Inc., Research Division - Senior Equity Analyst*

Okay. And then final question, on the NauticStar position the kind of plant production boost, where are you right now in terms of your goal of driving increased production at their facility? What's the ultimate goal? How would you like to exit fiscal '18? And any hurdles either operationally or CapEx wise to reach those?

Terry D. McNew - *MCBC Holdings, Inc. - President, CEO & Director*

So we are about 1 month ahead of our internal plan, Eric. Keep in mind, we own them. We purchased them and completed the transaction October 2, so we've owned them for about 4 months. But there are plethora of operational improvements underway. We reconfigured the plant in a much more organized and profitable flow. We are containing that to the CapEx budget for fiscal '18. We've made improvements in environmental health and safety, which you know we're very -- we put a very strong focus on. We will complete the facility reorganization by Q1 or within Q1 of model year '19. By the end of this fiscal year, we'll have about 75% of it completed. We've added additional resources in finance and HR functions as well, which is expected during the due diligence process, and we communicated that to you when we had our call on October 2. I think it's also important to note that we've not experienced any disruption at Mastercraft with the addition of NauticStar. We've had several people helping out with them, but both companies are operating extremely well. Their commissions, they have entire plant permitting at about 249 tons per year. We're consuming a little over about 52% to 55% of that currently. So given the same mix of product, we have quite a ways additional capacity. We broke the first constraint about a month ahead of plan in early December, and we increased count by 1 unit a day. We were targeting early January. We actually were able to do that in early December. Demand for the products continues to be strong as we communicated. It's one of the reasons we bought them, is the demand was higher than their supply. So we've -- we increased count in December, and we have plans to do that again in Q4 this fiscal year.

Operator

And our next question comes from Craig Kennison with Baird.

Craig R. Kennison - *Robert W. Baird & Co. Incorporated, Research Division - Director of Research Operations and Senior Research Analyst*

Wanted to follow up on the NauticStar conversation. I realize your focus today is on throughput and kind of operational excellence, which is a strong suit for you. Wondering to what extent you had a chance to look at the product road map. I know you've thought through that as it relates



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to Mastercraft. But are there opportunities for you to rethink where the product can go over the next 5 years now that you've got control of the asset?

Terry D. McNew - *MCBC Holdings, Inc. - President, CEO & Director*

Yes, absolutely, Craig. So Tim Schiek and many of us here at corporate have been working on adding additional dealers as well. The company, when we purchased them, had approximately 70 dealers, mostly east of the Mississippi. Add in Texas as well. We've already added a dealer in Canada, Australia, in western United States. We've already identified up to 59 additional opportunities for dealer expansion in the western United States. Our team here in sales and marketing at Mastercraft is assisting NauticStar, and we have a goal to increase the number of dealer locations within the next 12 months by about 20 additional locations over the 70-ish that were there when we purchased them. As far as the cycle plan, we have completed a 5-year cycle plan, the same as what we operate to here for product development at Mastercraft. And we have the first 2 years identified and locked in, and I -- as I say to you often and others, we don't announce the products that are coming out, but we have a couple of more products that will be introduced later in this calendar year.

Craig R. Kennison - *Robert W. Baird & Co. Incorporated, Research Division - Director of Research Operations and Senior Research Analyst*

And then as a follow-up to a point you made earlier, Terry, it sounds like the organization hasn't been taxed by the addition of NauticStar. In other words, you're able to continue your focus at Mastercraft. But I'm wondering if -- given all you had on your plate, is it fair to say that M&A is kind of off the table until you get NauticStar fully integrated?

Terry D. McNew - *MCBC Holdings, Inc. - President, CEO & Director*

We mentioned this before. In a perfect world, we'd love to be able to do a -- have a year in between acquisitions, but we, by no means, have been quiet. We, Tim and I, as we've said before, continue to evaluate several acquisition opportunities, and we're currently in the midst of doing that as well. And those take -- even if you are able to become the final bidder, it takes 3 to 4 months to complete due diligence. So we're doing well with NauticStar. We're 4 months into it, but we are currently evaluating other opportunities.

Craig R. Kennison - *Robert W. Baird & Co. Incorporated, Research Division - Director of Research Operations and Senior Research Analyst*

And then finally, Tim, following up on the tax issue. To what extent do you think you need to -- you have an opportunity to reinvest in the business given the tax windfall that materializes here?

Timothy M. Oxley - *MCBC Holdings, Inc. - VP, CFO, Treasurer & Secretary*

I think that's -- the way we answer that question is similar to the way we answer any of our excess cash that superior working capital management generates. And now we have in addition to that an excess generated by the tax rate decrease. During this quarter, the December ending quarter, we had \$17 million of additional principal payments we made on our term loan because the cash wasn't doing us any good sitting in the bank earning 0% interest. So we're going to continue to look at that as an opportunity to pay down debt. Obviously, it would be beneficial as we look at potential acquisitions, and we're just going to continue to evaluate those opportunities.

Terry D. McNew - *MCBC Holdings, Inc. - President, CEO & Director*

I might add, Craig, the third leg of that stool is we are continuing to invest in our portfolio.



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Operator

And our next question comes from Joe Altobello with Raymond James.

Joseph Nicholas Altobello - *Raymond James & Associates, Inc., Research Division - MD and Senior Analyst*

Just want to go back to the growth rates you guys mentioned earlier for both Mastercraft and NauticStar. It sounds like that accelerated a little bit this quarter from what you were doing. Is that being driven by any particular geography or any particular models? Or is that pretty broad-based? You guys did mention boat shows have been good to you so far and dealer traffic is up as well. Was just curious if that was a broad-based acceleration or any particular geographies or models.

Terry D. McNew - *MCBC Holdings, Inc. - President, CEO & Director*

It is very broad-based. I would suggest that our portfolio is as strong as it's ever been. Our XTs are selling extremely well. Our new XStar, as I mentioned, production rates are up 400% over the exit rate of the older XStar -- our XT22, it's been on market less than a year, is our strongest XT to date. The new XT25 is the highest visited portion of our website. So the NXT, so last year in January, we started our winner sales campaign with nationally advertised pricing. That has really accelerated those. They're selling extremely well, especially the NXT22. So our portfolio's extremely strong. And when you look at the -- every major region of the world is seeing positive growth now and we're growing along with it. Our year-over-year retail is outpacing the segment, so I think that's a function of all the work that the team's doing in terms of innovation. We've won about half of the NMMA's innovation awards for our segment in the last 4 years. It's just continuing to execute on what we do well. We spend a lot of time on product development and innovation and making sure that our stepladder pricing is correct. And we have, as we've mentioned before, the last 2 years, we've really spent a great deal of time working with our dealers on retail performance, and that is how -- we could spend hours on that, but that is a very disciplined approach. We spent a good deal of time on it at our dealer meeting in Orlando at -- in December, and we're clearly seeing stronger leads, more leads and diversity of leads from this process at our boat shows. We saw it last year. We're seeing it again with new dealers. So we started 2 years ago with a pilot group of 9 dealers. We've expanded it each year over the last 2 years, and we have about 65 dealers that participated in an active way, so good macroeconomic growth and extremely strong portfolio and better sell-through at the dealer level.

Joseph Nicholas Altobello - *Raymond James & Associates, Inc., Research Division - MD and Senior Analyst*

And then I guess, on NauticStar, if you were to exclude the manufacturing constraints right now, that business is growing high singles, low doubles. What would that growth rate be if you could keep up with demand?

Terry D. McNew - *MCBC Holdings, Inc. - President, CEO & Director*

We mentioned in our prepared remarks that they're seeing high single-digit to low double-digit growth along with Mastercraft. We are intentionally -- we've raised count. We plan on doing it again, but for the rest of this fiscal year, it's important that we continue to execute the changes, which are large changes to the production flow. They're done, follow up on it weekly with Tim Schiek. We're making good progress to that, and we're staying within our capital constraints. So model year '19, with the addition of additional dealers and the bulk of the facility layout will be done by the end of June, the remainder of it we've done by the end of the first quarter of next year, I really think those are going to start to increase the velocity of their throughput with additional dealers and the configuration done. And I would say that's nearly a permanent reconfiguration of the facility. I don't anticipate that being changed to -- really ever. We've laid it out in a way that we anticipate larger products so we can contain that as well as higher throughput. The constraint will most likely be omissions, which, again, given the current mix, just as an example, we could grow volume by an additional 40%.

Operator

And our next question comes from Michael Swartz with SunTrust.



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Michael Arlington Swartz - SunTrust Robinson Humphrey, Inc., Research Division - Senior Analyst

Just, Terry, some clarification. Maybe around the production rates, I think, you were talking about the XT25 and you said they're about, what, 400% larger than the product before it, I guess, during the [cycle].

Terry D. McNew - MCBC Holdings, Inc. - President, CEO & Director

Michael, that was the XStar. The new XStar.

Michael Arlington Swartz - SunTrust Robinson Humphrey, Inc., Research Division - Senior Analyst

That was the XStar -- the -- okay. Could -- just a little more context on that. How old was the XStar, I mean, granularity from a volume basis maybe?

Terry D. McNew - MCBC Holdings, Inc. - President, CEO & Director

So the previous XStar was completing its fifth year, so it was about a strong 4.5 years. Our typical product life cycle is 4 years, and its volume had been around 60 units to 75 units annually on its exit rate. So we're going to be up 400% from that.

Michael Arlington Swartz - SunTrust Robinson Humphrey, Inc., Research Division - Senior Analyst

And then just the next question be on -- I think you made the commentary around -- something was up 20% coming out of the boat shows you've seen to date. Was that orders? Was that indications?

Terry D. McNew - MCBC Holdings, Inc. - President, CEO & Director

These were retail sales that we track every single year, so we have a list of the top, want to say, 50-ish boat shows around the world, and we track those every year. We're looking at retail sales, so we track the number of retail sales through the end of the show plus 2 weeks follow-up. So they're following up on leads that they may have gathered at the show. And that's the way we've consistently measured it, and so for the shows that have completed, the show plus 2 weeks of follow-up, we are up 20% in retail sales for those shows compared to the same level last year.

Timothy M. Oxley - MCBC Holdings, Inc. - VP, CFO, Treasurer & Secretary

And Mike, that can include a dealer selling their boat that's going to be produced in the future. We love seeing a boat going down the line that has not only a dealer's name, which it always has a dealer's name, but a retail customer's name as well because those boats fly right through the pipeline, and it's very healthy when we see that.

Terry D. McNew - MCBC Holdings, Inc. - President, CEO & Director

So combination of what the dealer has on hand plus deposits for orders. And I don't know if I mentioned it but retail names are growing rapidly. In fact, we contacted all of our dealers twice in the last 2 weeks and just reiterated when they put their orders in, be sure their retail names are on there because we're going to pull those up and prioritize those in the production plant. We are sold out through the end of this model year on a wholesale basis.



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Michael Arlington Swartz - *SunTrust Robinson Humphrey, Inc., Research Division - Senior Analyst*

Okay, great. And then just final one for me. Just heard some chatter, I guess, earlier this year and late last year that you're dropping some, I guess, new dealers in some of your trade areas where you have existing dealers. Can you talk about maybe the strategy there and maybe how you contain some of the risks of doing that?

Terry D. McNew - *MCBC Holdings, Inc. - President, CEO & Director*

Yes. So as we've said on many of these quarterly earnings calls, really, for the last 5 years, each year, we sit down our sales and marketing staff, Tim and I, if needed. We visit dealers, and we work on their business plans. We show them where every retail sale is, not only for us but for every competitor in their region. So our strategy is to try to give more dealers as large a territory as possible where they can still effectively service and sell. Data clearly shows, over the last several years, where there are -- the dealers generally were doing really well in their -- around their store location, but their territory was far larger. So we've encouraged dealers to add locations. And they've been very effective. We mentioned this one many times in the past. Our Dallas/Fort Worth area took advantage of this about 3 years ago, added a satellite location in the Dallas area. Their primary store's in Fort Worth. Long story short, they doubled their business within 18 months. So there are areas though where some dealers just didn't have the desire or the fortitude, whatever it was, but we gave them plenty of time and -- a couple years and said, at some point, we are missing sales and we're well below market share and we need to add an additional location in that territory. And so we have done that over the last 18 months. We are now up to 240 dealer locations throughout the world. You have some concern. There's kind of a myriad of some people get it, they understand it, some don't. There have been some turnover, but it's been fairly -- I mean, it's been well contained. The turnover has been very de minimis, and we're progressing really well.

Operator

And our next question comes from Tim Conder with Wells Fargo Security.

Timothy Andrew Conder - *Wells Fargo Securities, LLC, Research Division - MD and Senior Leisure Analyst*

Terry, maybe a little bit more color. Regionally, you said that things were pretty strong everywhere seeing kind of synchronized global growth, but Canada, it would seem like that, that has an opportunity to really accelerate this selling season for the industry. So maybe a little more color there. And then on the shipping, anything that you guys are trying to do to mitigate those costs? Or I mean, we're hearing shortages on shipping, tight supply across many industries. Any additional color there? And then the other piece would be on the consumer through the shows. I think, Tim, you mentioned that the tax cut should also help the consumer. Any hard evidence of that, consumer feedback saying, "Yes, I'm going to have some more money here. That's why I'm going to go ahead and pull the trigger on buying the boat here."?

Terry D. McNew - *MCBC Holdings, Inc. - President, CEO & Director*

Let me take your first question, and I'll throw over item 2 and 3 to Tim. But Texas, as you know, is the largest NPA for ski, wake. It's about 2x larger than California and Michigan, which are close #2 and #3. We continue to increase in share in Texas and do really well. As I mentioned Dallas/Fort Worth has doubled business in the last 24 months. California, we've added dealers. That is going extremely well. Our northern California long-time dealer, Norcal, continues to do well. And we've mentioned this before, in both states, we were underpenetrated, under our national average for market share. So we're improving well there. Michigan, we have the highest market share of any fiberglass boat, so we continue to -- Action Watersports continues to do extremely well. Northeast is doing good. Southeast is doing good, and one thing that we're very excited about is Action Watersports is now our dealer in the Orlando area. They purchased the former USA Water Ski Hall of Fame right off I-4 just west of Disney. They're doing a soft opening. Well, they did last month, and they'll be -- in the next 6 months, they're doing some construction. But they're in an incredibly efficient and effective retailer, so we are looking forward to capturing market share in Florida. So when you talk about Canada, I'll remind you, 2 years ago, Tim and I -- when the Canadian dollar devalued pretty rapidly, not quite, but almost 2 years ago and at the same time, oil prices dropped dramatically. So Western Canada, as you know, is very commodity driven, very oil based. We didn't throw money at it. We took the commitments in our dealers in Canada down 30% to 50% in model year '16. They were very appreciative of it, saved us dollars. But traditionally,



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Canada had been about 15% of our wholesale volume. U.S. had been about 70%, rest of the world about 15%. So during that time in '16, our U.S. volume became about low 80%. Canada dropped down to about 11%. The rest of the world was about 8%. In '17, we started seeing Canada return, and now in model year '18, they are back to their traditional, about 15% of our wholesale business. So we're very comfortable with that, and we continue to see opportunities for growth, to your point, in Canada. And that was a, we think, absolutely the right thing to do. And we've been very, very profitable and seeing our sales not only in wholesale but at retail improve dramatically in Australia. We're up significantly there. And now we're starting to see Europe finally coming back. So as I mentioned in the prepared remarks, every area of the world is performing really well.

Timothy M. Oxley - *MCBC Holdings, Inc. - VP, CFO, Treasurer & Secretary*

I think on the weakening dollar, certainly, it provides a tailwind, but in most cases, the dealers kind of have to work through the inventory that was purchased when the dealer was strong -- when the dollar was stronger. So I think that we're going to see continued momentum in international markets, not only in Canada but in Europe and Australia as well. In regard to your comment on shipping, we're not seeing any problems. We have a -- kind of a local supplier that has been able to keep up with our demands, and we'll just keep a close eye on that. But we don't have anything right now that we're concerned about affecting shipping. As to the consumer, I think that the data that points to consumers being bullish and driving the retail demand, we're seeing more, more of the slots having consumers' names, which means that they're custom ordering their boat, tends to have a bit more of the bells and whistles on the boat and an indication that consumer sentiment is more bullish. And so rather than take the boat on the showroom floor, they're going to go ahead and order a -- custom order one with all the bells and whistles. So because we're seeing that increasing, I think that's an indication that we're seeing the retail being driven by some of the tax change.

Timothy Andrew Conder - *Wells Fargo Securities, LLC, Research Division - MD and Senior Leisure Analyst*

Okay. And then gentlemen, just to revisit the, I think, the prior question that was asked on the tax benefit, allocation of that bucket. You guys paid down some debt here, and you're looking at other M&A opportunities. Can you kind of maybe just, percentage wise, bucket that out? I know M&A may or may not happen. So let's say it doesn't happen, would you let that flow to the bottom line, initiate a dividend? Would you accelerate debt repayment, further internal acceleration of projects? Just a little bit more expansion on your prior comments.

Terry D. McNew - *MCBC Holdings, Inc. - President, CEO & Director*

Let me start on that, Tim. You can finish. But I can tell, we were not contemplating a dividend. We just don't think that's right. We're a growth company. That might happen later on in our life, but we are certainly investing in our product portfolio. We've grown the lower end of it. We think there's room for growth beyond what we have today. I would say that, that's, to put in percentages, maybe an additional 25% to 30%. Certainly, M&A activity is an opportunity, but we don't know if and when those happen. So I think the largest bucket is certainly debt repayment, and as Tim mentioned, we paid down, what, \$17 million in Q2, and we have additional plans to do that [if we want].

Timothy M. Oxley - *MCBC Holdings, Inc. - VP, CFO, Treasurer & Secretary*

Right. And so if we use the disposable cash to pay down debt, all that does is give us additional debt capacity over and above of where it is today. Our leverage at the end of December was about, I think, it was a little bit less than 1.5x adjusted EBITDA. So it's a very -- we're very lightly levered. We'll continue to delever rapidly as we generate cash, and we're going to do that as long as there's not a better opportunity that comes along.

Operator

And our next question comes from Laura Engel with Stonegate Capital.



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Laura Shelmire Engel - *Stonegate Capital Markets, Inc., Research Division - Senior Research Analyst*

I wonder if you could give us any feel for the -- maybe looking longer term, quantify how much improvement you might be able to see with the NauticStar operations and everything you've invested and all the changes you're making. Longer term, what [comp] was that? When might you see that out of the teens and into the 20s?

Terry D. McNew - *MCBC Holdings, Inc. - President, CEO & Director*

Well, we've said when we purchased them on our call in October 2, we feel, eventually in time, we can drive their gross margins from the high teens into the low, perhaps, even the mid-20s. That'll take some time. But the first step was getting the facility layout done. So consider that to be done in about 7 to 8 months. Adding dealers is going to be critical. That's certainly opportunity. As we said, it's a volume opportunity for us. There are a lot of dealers that are showing interest in NauticStar. We feel like there's an extremely strong probability that we will sign 20 additional dealers within the next 12 months. In fact, we're already about 5 towards that. So it's certainly a great brand, 3 great categories: bay boats, center consoles and deck boats. The demand for center console and deck boats is extremely strong. But I don't want to underplay the bay boats. That is about nearly 30% of their volume, and they have very strong market share. I think they're in the 18- to 28-foot category. They're a leader -- they're 1, 3 and 5 in terms of market share in that size range for bay boats, deck boats and center consoles, respectfully. So we see a very strong top line continuing for the next couple of years.

Operator

And our next question comes from Rommel Dionisio from Aegis.

Rommel Tolentino Dionisio - *Aegis Capital Corporation, Research Division - MD*

Terry, I think you touched on -- regards to Tim's question, but maybe just ask for a little more detail on Europe. That market picking up economically, just curious if either of you guys went to the Düsseldorf show this year a few weeks ago. Any feedback you're hearing from that? And also, can you just remind us, where are you from a dealer distribution perspective in terms of how can you take it -- how quickly can you take advantage of that market if and when it comes back? Sounds like it's already picking up. And if additional investments are required there to sort of boost your marketing infrastructure in that market?

Terry D. McNew - *MCBC Holdings, Inc. - President, CEO & Director*

Well, we've signed additional dealers over the last couple of years everywhere in the world, including Europe and Middle East. So we've got very strong dealers there, and we're continuing to look for opportunities in several places around the Mediterranean. But we feel very comfortable. We feel very well represented in there. We're just going to continue to add to that growth. The GDP, I think, right now for Europe is forecasted in the low to mid-2% range, so that's certainly positive relative to the last few years. And our dealers, I know, Tim, you were over at Düsseldorf. Maybe you can comment on that.

Timothy M. Oxley - *MCBC Holdings, Inc. - VP, CFO, Treasurer & Secretary*

Yes. One of the things that impressed me about the Düsseldorf show is we had consumers from all over Europe, and therefore, we have dealers from all over Europe represented there in our corporate booth. And there wasn't any particular region that stood out. It was that overall demand across the continent that was really impressive to me. And so keep in mind that because we do work 4 10-hour shifts a week, that gives us ability to flex up if the demand kind of spikes unexpectedly, and if we -- we can drive additional output that way without having to wait to hire the people and get them trained. So we've got a pretty flexible manufacturing process, and that should give us an opportunity to take advantage of any unexpected short-term event.



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Operator

And our next question comes from Dan Charrow with KeyBanc.

Daniel Charrow - *KeyBanc Capital Markets Inc., Research Division - Associate*

Dan Charrow here on for Brett Andress. So it seems like MasterCraft growth trends kind of outperformed NauticStar at least in the first half. Do you guys expect that to continue looking into the back half of your fiscal?

Terry D. McNew - *MCBC Holdings, Inc. - President, CEO & Director*

Mastercraft, obviously, is a larger company with a far greater dealer network. We have about 150 dealers worldwide with 240 locations, and we're in approximately 40 countries around the world. So we're in the midst of growing NauticStar. It's just an eastern U.S. company. So that takes a little bit of time. We're well on our path. But we believe that both companies in unit growth, second half as I mentioned, will, on a full year basis, still be up about high single to low double digits. And we are not pushing that. I must say -- I just want to reemphasize that our dealer terms are improving all the time. I mean, they've been good for a while, and they just continue to get better and better. We are very much a pull system, not a push, and I think, Tim, you can -- I think you did in your prepared comments say that the promotional activity in Q2 was pretty benign.

Timothy M. Oxley - *MCBC Holdings, Inc. - VP, CFO, Treasurer & Secretary*

Right. I do think that since Mastercraft is a little more mature operationally, we're going to be able to take advantage of the demand and probably respond more efficiently than NauticStar. So that may hold them back a little bit, but keep in mind that both companies are healthy and growing very well.

Terry D. McNew - *MCBC Holdings, Inc. - President, CEO & Director*

NauticStar is in their evolution where MasterCraft was 5 years ago. So they're doing facility layout and changes. They're focusing on EHS. They're focusing on dealer development. So they've got a lot of things going on, and they're well on track to do it. They're just a little less mature than Mastercraft. But I -- we are forecasting very strong second half.

Operator

And I'm not showing any further questions at this time. I would now like to turn the call back over to President and Chief Executive Officer, Terry McNew, for any further remarks.

Terry D. McNew - *MCBC Holdings, Inc. - President, CEO & Director*

Thank you, operator, and once again, thanks to everyone for joining us this evening. Across the organization, we're well positioned for fiscal 2018 and beyond, and we look forward to updating you on our progress and third quarter results in May. Thank you.

Operator

Ladies and gentlemen, thank you for participating in today's conference. This does conclude today's program, and you may all disconnect. Everyone have a wonderful day.



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