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Twin Disc, Inc.

Fiscal Second Quarter 2020 Earnings Conference Call

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C O R P O R A T E P A R T I C I P A N T S

Stan Berger, *SM Berger & Company, Moderator*

John H. Batten, *Chief Executive Officer*

Jeffrey S. Knutson, *Vice President of Finance, Chief Financial Officer, Treasurer and Secretary*

C O N F E R E N C E C A L L P A R T I C I P A N T S

Noah Kaye, *Oppenheimer*

Tim Wojs, *Robert W. Baird & Co.*

Rand Gesing, *Neuberger Berman*

Simon Wong, *G. Research*

P R E S E N T A T I O N

Operator

Good day and welcome to the Twin Disc Fiscal Second Quarter 2020 Financial Results Call. Today's conference is being recorded.

At this time, I would like to turn the conference over to Stan Berger. Please go ahead, sir.

Stan Berger, *SM Berger & Company, Moderator*

Thank you, Christine. On behalf of the Management of Twin Disc, we are extremely pleased that you have taken the time to participate in our call, and thank you for joining us to discuss the Company's Fiscal 2020 second quarter and six-month financial results and business outlook.

Before I introduce Management, I would like to remind everyone that certain statements made during this conference call, especially those that state Management's intentions, hopes, beliefs, expectations, or predictions for the future are forward-looking statements. It is important to remember that the Company's actual results could differ materially from those projected in such forward-looking statements. Additional information concerning factors that could cause actual results to differ materially from those in the forward-looking statements are contained in the Company's Annual Report on Form 10-K, copies of which may be obtained by contacting either the Company or the SEC.

By now, you should have received a copy of the news release which was issued this morning before the market opened. If you have not received a copy, please call Annette Mianecki at (262) 638-4000 and she will send a copy to you.

Hosting the call today are John Batten, Twin Disc's Chief Executive Officer, and Jeff Knutson, the Company's Vice President of Finance, Chief Financial Officer, Treasurer and Secretary.

At this time, I will turn the call over to John. John?

John H. Batten, *Chief Executive Officer*

Thank you, Stan, and good morning, everyone. Welcome to our Fiscal 2020 second quarter conference call. As usual, we will begin with a short summary statement, and then Jeff and I will be happy to take your questions. Before Jeff goes over the quarter results, I'll touch on some of the operational highlights from the quarter.

As we mentioned in prior calls, we've been addressing cost issues on some of our marine and transmission models due to forces buyer changes during the oil and gas run-up in Fiscal 2018 and '19. In order to meet demand on other products, we had to move supply to other vendors, and not always at a lower cost. We made significant progress in the quarter in proving out many new parts from new suppliers, and actually had a few go into production.

To date, we have identified over $1 million in savings for Fiscal 2020 spread out just over three models, and we expect to continue to add to this as more components are approved. Assuming a static mix and volume going forward (inaudible), we expect margins to continue to improve over the next four to eight quarters as we bring many new supply sources online. We've also begun to work with a key outside partner to help us identify and to validate more suppliers in the Asia Region.

In the quarter, we also offered an early retirement package to our employees in our Domestic Operations, and we've reduced our Domestic headcount by about 10% for about another $1.8 million savings, a $1 million savings in the second half of the year.

As demand in our market improves, some of this lost capacity will be added to our Lufkin facility as it comes online this summer. We continue to address other cost drivers on a global basis, such as nonessential overhead, and to make the necessary adjustment.

One bullet that probably stood out in the release was the partner cancellation of the Marine Propulsion Program. We wish the outcome were different, but it isn't the end of the story. This is an accounting moment in time and also the end of any charges for White House. This program may continue in another form.

Now I'll turn to a couple of our strategic objectives for a moment as that acquisition continues to surpass their expectations and to be the focal point for our diversification effort. Backorders and active projects in Asia and North America continue to grow. One of our more recent applications, the Maid in the Mist at Niagara Falls, an all-electric ferry boat that is getting a lot of attention, and you should see more coming in the near future with the integrated L-drive from Veth Propulsion.

The cross-pollination between Veth and Twin Disc continues to drive our hybrid strategy in our other market as we develop both component and system solutions as our markets continue to evolve.

In terms of capacity planning for the full cycle, including the ups in Oil and Gas, we told you that we have moved our North American aftermarket business to a standalone facility along the I-94 corridor between

Milwaukee and Chicago. That facility has been up and running since last summer, and we're running more efficiently in terms of manhours per shipment than we were when we were in the factory. Vertical lift modules in a layout dedicated to parts is making the operation much more efficient. Currently we are using the facility as a depot location for our marine transmissions coming in from our European operations.

Our facility in Lufkin, Texas is nearing completion, and we should take occupancy in our Fiscal Fourth Quarter with the first shipments in the first quarter of Fiscal '21. We have begun a limited hiring program in Texas and identified key personnel from the scene who will move to help get the plant operational. Access to a growing talented North American labor force is critical to our growth objective. Shipments from the plant should grow throughout Fiscal '21 as we ramp up different models for production.

Finally, in our main facility in Wisconsin, we've begun a new Sales and Operations Planning Program to retool our processes and how we run our business. With the downturn of 2015, recent retirements, and all of our new hires in the past two years, it is the perfect time to reset and to best utilize our new cap ex spending and freed-up floorspace. This is an 18-to-24-month journey that we kicked off earlier this month.

With that, I'll turn it over to Jeff for some comments on the financials.

Jeffrey S. Knutson, *Vice President of Finance, Chief Financial Officer, Treasurer and Secretary*

Thanks, John, and good morning, everyone. I'll briefly run through the Fiscal ’20 second quarter numbers.

Sales of $59.5 million for the quarter were flat with the previous quarter, and down $18.6 million, or just under 24% from the prior year second quarter. The quarter decline is primarily the result of significant reduction in new-build and aftermarket activity in the North American fracking market, along with the (inaudible) in the global marine and industrial market.

The oil and gas decline accounted for $16.5 million in the second quarter reduction in sales and is a continuation of the slowdown we saw in the fourth quarter of Fiscal '19. Through the first half sales are now down $34 million, or 22.2% compared to the prior year, with foreign currency exchange contributing $2.6 million to the decrease.

Second quarter margin percent was 26.4% compared to 33.4% in the prior year second quarter. Our gross margin performance for the quarter was again severely impacted by a continuation of the unfavorable product mix which began in the Fiscal '19 fourth quarter, with lower fracking demand for new rig construction and reduced aftermarket demand being the primary drivers.

Gross profit percent for the second quarter is improved over the first quarter of 16.3% in the fourth quarter of Fiscal '19, which was 22.7%. This improving trend is the result of targeted cost reduction actions done in key products and overall focus on cost containment and production efficiency. As we discussed in the Year End '19 Earnings Call, we anticipated a continuation of this difficult sales mix and have been focusing on cost reduction and pricing actions to drive margin improvement. We expect to see a continuation of this positive trend through Fiscal '20.

Spending on marketing, engineering, and administrative costs for Fiscal '20 second quarter decreased $2.5 million, or just over 13% compared to Fiscal '19. The decrease is a result of reduced bonus, marketing spending, stock-based comp, and professional fees, along with the impact of the Mill Log sale, which happened in the third fiscal quarter of last year.

With the oil and gas markets struggling over the past three quarters, we've aggressively pursued cost-reduction opportunity to compensate for the decline in gross profit.

A restructuring charge of $4.2 million was recorded in the second quarter. This charge included $3.2 million related to the partner-driven termination of a marine propulsion program for which we had provided development and production services. This $3.2 million charge was comprised of $2.2 million in non-cash write-off of assets and a $1 million cash accrual to settle a supplier commitment associated with the program.

In addition, we recorded about $1 million in restructuring charges related to headcount reductions at our Domestic and European Operation. As John noted, those reductions will generate just over $1 million of savings in the second half and a little over $2 million on an annualized basis.

With the reduced second quarter volume, challenging product mix, and the significant restructuring charges, we reported an operating loss of $5 million in the quarter compared to a $6.7 million operating profit in the Fiscal '19 second quarter. Through the first half operating profit has declined by $23.4 million to a loss of converted (phon) operating profit of $11.6 million in the prior year.

The Fiscal '20 first half includes the $4.4 million of restructuring charges and the $3.9 million product performance charges we recorded in the first quarter.

The effective tax rate for the Fiscal '20 first half was just 4.3%, significantly lower than the current year rate of 25.1%. The current year rate was significantly impacted by the guilty (phon) provision of the Tax Cut and Jobs Act which requires the inclusion of foreign income but prohibits certain foreign deductions (inaudible) domestic loss position. The guilty inclusion decreased the first-half tax rate by 18.6%. The net loss for the second quarter of Fiscal '20 was $6.5 million or $0.49 per diluted share compared to a net profit of $4.1 million, or $0.31 per diluted share in the prior year second quarter. Year-to-date, the net loss was $12.8 million or $0.98 per share compared to a net profit of $6.9 million or $0.50—$0.56 per share in the Fiscal '19 first half.

Negative EBITDA of $2 million for the quarter is down from a positive EBITDA of $9 million the prior year second quarter. For the first half, EBITDA is now a negative $6.6 million compared to $17.1 positive EBITDA for Fiscal '19 first half. Most recently, declines in EBITDA resulted in a slight increase in debt levels. We anticipated the likely issue in maintaining compliance with the debt in EBITDA covenant in our credit (inaudible).

We began discussions with BMO during the quarter and were able to close the third amendment to the credit agreement on January 28. This amendment provides temporary covenant relief as we work through the current market challenges. Under this amendment we finished the quarter with a debt-to-EBITDA ratio of 3.11% which was well within the revised covenant requirement of 4.0%.

Inventory was up $7.4 million in the quarter as reduction efforts were hampered by the reduced volume and vendor commitment. Two-point-three million dollars of this increase was related to the termination of the Propulsion Program as percentage of completion accounting resulted in a $2.3 million cumulative credit balance in the inventory at the time the program was cancelled.

With no inventory improvement and significant capital spending, free cashflow with negative $4.2 million in the quarter, driving a $3 million increase in debt. Six-month backlog finished the quarter at $94.7 million, which is down just slightly from the $100 million at the end of Fiscal '19.

Operating cash flow was slightly positive for the first half, $3.9 million better than the prior year first half despite significantly reduced earnings and an increase in inventory.

Cap ex levels remain relatively high as we execute on some key investments in machinery and equipment. We expect to spend between $11 million and $13 million this year as we invest in modern machine and quality technology to drive productivity and cost improvements.

Now I'll turn it back to John for some final comments.

John H. Batten, *Chief Executive Officer*

Sure. Thanks, Jeff. Now I'll spend a quick moment on the outlook.

The second half of Fiscal 2020 still faces some of the same domestic oil and gas challenges of the first half. We are seeing aftermarket signals of life across a broad range of markets including oil and gas. We are seeing increased rebuild activity, and hope that this continues throughout the remainder of the Fiscal Year. A disappointment in the second quarter was the rapid drop in industrial demand. Speaking with suppliers, this happened across the market. Early signs in January are positive, backed up by increased aftermarket orders.

We have the backlog to make our third quarter better, a better quarter in terms of revenue and margins, and provided the recent coronavirus outbreak doesn't dramatically affect our customers in Asia, the fourth quarter should also see that improvement trend continue. We don't see any domestic new-unit demand in oil and gas until this summer.

That concludes my prepared remarks, and now Jeff and I will be happy to take your questions. Christina, could you please open the line for questions?

Operator

Yes. Thank you. If you would like to ask a question, please signal by pressing star, one on your telephone keypad. If you are using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. Again, press star, one to ask a question.

We'll take our first question from Noah Kaye with Oppenheimer.

Noah Kaye, *Oppenheimer*

Thank you and good morning. Stripping out year-over-year restructuring, it looks like EBITDA (inaudible) got back to a (inaudible) normal level and you improved the gross margin sequentially (inaudible) mention (inaudible) to take out cost. I'm just trying to understand how the further cost reduction effort vis-à-vis your commentary around potential improvement in the back half in activity, which levers are you going to continue pressing on? Are any costs likely to come back, the improvements that you foresee in some markets? Just help us get through a (inaudible) those factors (inaudible).

John H. Batten, *Chief Executive Officer*

Sure. Noah, it's John. It's got two parts. Well, three parts. We're going to continue the material variable costs coming in, finding new suppliers. The second one is operational improvements in our domestic operations, getting industrial out and down to Texas, reorganizing the plant here, being more efficient with our processes. But then there's still a component outside of North America that is a fixed-cost rationalization. We're actively working on all three of them.

Noah Kaye, *Oppenheimer*

Okay. That was helpful. Then to be clear, you said at the end of your prepared remarks, you're not expecting North America oil and gas transmissions, certainly not the (inaudible) market to come back any time soon, correct?

John H. Batten, *Chief Executive Officer*

I think we could see some orders in this fiscal year, but my gut tells me there won't be any shipments this fiscal—there won't be any significant shipment this fiscal year. But that …

Noah Kaye, *Oppenheimer*

Right. If I could ask on the determination of that Marine Propulsion Program. Can you just give us a little bit of color on that, with that legacy twin program. Was that a debt program? How to understand that …

John H. Batten, *Chief Executive Officer*

It was …

Noah Kaye, *Oppenheimer*

(Inaudible)

John H. Batten, *Chief Executive Officer*

Sure.

Noah Kaye, *Oppenheimer*

(Inaudible)

John H. Batten, *Chief Executive Officer*

That's a pro—yes. It's John again. It's a program that we announced close to eight years ago, maybe more, with an engine OEM here in North America. Their strategy has changed and so the program was cancelled. We never got into production. Part of the charge is—if there's a continuation where we continue on, a lot of it, it will have our name on it. There's a clause here, and a lot of the charges reflect that. We can't continue on with another name on it. It's not the end of the story, Noah. I hope I have—certainly there's a chance that there's a release before the third quarter conference call, but certainly by the third quarter conference call have to have—I hope to have the rest of the story here for you.

Noah Kaye, *Oppenheimer*

I'll check that. I'll jump back in queue.

John H. Batten, *Chief Executive Officer*

Okay.

Operator

We'll take our next question from Tim Wojs with Baird.

Tim Wojs, *Robert W. Baird & Co.*

Hey, hey, good morning, guys. Close enough.

John H. Batten, *Chief Executive Officer*

Hey, Tim.

Tim Wojs, *Robert W. Baird & Co.*

Maybe just, in the back half, as you're thinking about some of the Asian orders that you got and maybe some of the increments you've seen in marine, how big of a revenue ramp do you think we can see in the back half of the year? We'll maybe use this $59 million to $60 million run rate in the first half as a base.

Jeffrey S. Knutson, *Vice President of Finance, Chief Financial Officer, Treasurer and Secretary*

Yes. Yes. This is Jeff. John and I—just a sidebar, we were thinking 15% is what is anticipated.

Tim Wojs, *Robert W. Baird & Co.*

From the first half?

Jeffrey S. Knutson, *Vice President of Finance, Chief Financial Officer, Treasurer and Secretary*

Yes.

Tim Wojs, *Robert W. Baird & Co.*

Okay, okay, gotcha. Okay. How big was the—I think in the press release you had mentioned some production delays that had impacted shipments. How big was that? Was that material?

Jeffrey S. Knutson, *Vice President of Finance, Chief Financial Officer, Treasurer and Secretary*

Yes. The way we quantify that, it's about $6 million that could have gone out had we been able to get the materials that we needed to do the assembly and enable to ramp up our assembly to where we expect we should be. It's about $6 million impact in the quarter.

Tim Wojs, *Robert W. Baird & Co.*

Okay. That would be included in the—that would really (inaudible) in the third quarter.

Jeffrey S. Knutson, *Vice President of Finance, Chief Financial Officer, Treasurer and Secretary*

Yes.

Tim Wojs, *Robert W. Baird & Co.*

Okay, gotcha. Okay. Then, I guess, just on some of the restructuring in the voluntary retirement comments that you made, John. Is there going be some shifting of the workforce, structurally from Racine down to Texas, because I guess from what we've seen over the last couple of years, it's been hard for you to find people in Racine. I'm just curious about, maybe some color on the background of the voluntary retirement.

John H. Batten, *Chief Executive Officer*

Yes, it's—I mean, the timing is right on two fronts. We had excess capacity in terms of people in Racine who are near retirement, at retirement age, and we have a plant coming online down in Texas. You're absolutely right. We take the early retirement, and we've got a lot of people with a lot of knowledge leaving. We can handle the production that we have right here, but as as we—as Lufkin comes online, you're absolutely right. The hiring and replacing of those bodies, a lot of that's going to happen in Texas.

Tim Wojs, *Robert W. Baird & Co.*

Okay.

John H. Batten, *Chief Executive Officer*

Again, we're very optimistic. One of the reasons we chose Lufkin was specifically because of their labor pool down there.

Tim Wojs, *Robert W. Baird & Co.*

Okay.

John H. Batten, *Chief Executive Officer*

With the quality of employees that we've been able to find down there.

Tim Wojs, *Robert W. Baird & Co.*

Okay, okay. Then, Jeff, what kind of gross margin level do you think we can exit the year at? Then, as you look at 2021 as Lufkin comes up, is there any under-absorption or anything like that that we should be aware of?

Jeffrey S. Knutson, *Vice President of Finance, Chief Financial Officer, Treasurer and Secretary*

Yes. I think—we've been targeting, I think we said last quarter as well, to get to the high 20s as we exit the year, assuming no significant change in mix. Any change in mix would probably be a good guy. I think we will, as we wind down maybe some activities that are being moved to Lufkin, and ramp up Lufkin, I think we might have some (inaudible) absorption in the first quarter (inaudible).

John H. Batten, *Chief Executive Officer*

(Inaudible) increased expense in moving. But I think it will improve. It will definitely take a little bit of—it will be a drag for the first few quarters as we—because we can't just—Q1 of whatever in the first quarter, we won't be shipping 100%. We'll be bringing it up slowly.

Tim Wojs, *Robert W. Baird & Co.*

Right.

John H. Batten, *Chief Executive Officer*

We want to do it right.

Tim Wojs, *Robert W. Baird & Co.*

Okay, okay. That makes sense. Then, I guess just from an SG&A perspective, if you're at this level of revenue, would you expect a $15 million, $17 million level for SG&A to be pretty consistent or sustainable?

John H. Batten, *Chief Executive Officer*

Yes, I think so. I mean, within that range, plus or minus a couple percent, yes.

Tim Wojs, *Robert W. Baird & Co.*

Okay. All right. Then, last one, do you think just with inventory you'll be able to generate positive free cashflow for the rest of the year?

John H. Batten, *Chief Executive Officer*

I'm glad you asked that, Tim, because I was going to interject that (inaudible) you asked the question. I'm glad you asked that. The jump was a bit of a shock to me and, again, I didn't foresee the negative inventory reversal from the Marine Propulsion Program. But inventories at our factory, primarily here in Racine, actually went down in the quarter. We had a lot of stuff shipped from factories in December that did not make the quarter cutoff. They're either in transit or they got to our distributors, our company-owned distributors, and we don't—and they haven't gotten to the customer yet. I think the trend that you will see during the remainder of the second half of the year will be an improving trend.

Tim Wojs, *Robert W. Baird & Co.*

Okay. I mean, it sounds like …

John H. Batten, *Chief Executive Officer*

First (inaudible) the factory …

Tim Wojs, *Robert W. Baird & Co.*

Yes.

John H. Batten, *Chief Executive Officer*

We've got a (inaudible) down at the factory and it's getting to the customer.

Tim Wojs, *Robert W. Baird & Co.*

Right. I mean, it kind of marries with what you're saying on some of the production delays, that $6 million you called out. That's probably in transit, and that's probably pretty decent inventory that's going to flush out, so …

John H. Batten, *Chief Executive Officer*

There's a big chunk of it in transit right now.

Tim Wojs, *Robert W. Baird & Co.*

Okay, okay, great. Appreciate the time. Good luck, John, and the rest of you guys. Thanks.

John H. Batten, *Chief Executive Officer*

Thanks, Tim.

Operator

We'll go to our next question from Rand Gesing with Neuberger Berman.

Rand Gesing, *Neuberger Berman*

Hey, guys.

John H. Batten, *Chief Executive Officer*

Hi, Rand.

Rand Gesing, *Neuberger Berman*

On that last question, can you be a little bit more specific? I mean, can we generate $10 million in operating cashflow for the second half? Given (inaudible) and you've got inventory coming out. I mean, I would like to see some flesh.

John H. Batten, *Chief Executive Officer*

Yes, $10 million might be on the high side. I think operating cash, we should definitely be positive in the second half. Free cash, I'd like to say we will be positive in the second half. We do have cap ex which we're about, call it, halfway through what we thought we would spend, so I think in that $7 million to $9 million of operating cash and maybe $1 million to $3 million in free cash in the second half is what I think we might expect.

Rand Gesing, *Neuberger Berman*

Okay. Some of the (inaudible). I know (inaudible) the company but you do have a sense (inaudible) of the revenues there at the time?

John H. Batten, *Chief Executive Officer*

Rand, you cut out a little bit on the first part of the question.

Rand Gesing, *Neuberger Berman*

Yes. On the acquisition (inaudible), the new acquisitions (inaudible).

John H. Batten, *Chief Executive Officer*

Yes.

Rand Gesing, *Neuberger Berman*

What are the revenues there? I'm assuming it's a mid-single digit growth.

Jeffrey S. Knutson, *Vice President of Finance, Chief Financial Officer, Treasurer and Secretary*

Yes. The revenues for the first half were around $23 million, $24 million. I would say the first half, they're very project-oriented, so their shipments come in big chunks.

Rand Gesing, *Neuberger Berman*

Right.

Jeffrey S. Knutson, *Vice President of Finance, Chief Financial Officer, Treasurer and Secretary*

The first half was kind of flat compared to the previous year. I think what we have a lot of optimism around is the activity, order activity, in particular in North America, that we're seeing right now driving growth in the—as we get into Fiscal '21.

Rand Gesing, *Neuberger Berman*

Okay. Obviously, you've had a bit of a weak (inaudible) strung out throughout the whole revenue (inaudible) I think. But is that the case that some of your end markets are weak or just characterize that for me.

John H. Batten, *Chief Executive Officer*

Okay. Yes, I think so. There are no end markets right now that are growing beyond 1% or 2%, and there's weakness, I would say, across both of them. Yes, there are a few bright spots. Stable is about as good as it gets right now. I would say the …

Rand Gesing, *Neuberger Berman*

Hi guys, can you hear me?

John H. Batten, *Chief Executive Officer*

Yes.

Rand Gesing, *Neuberger Berman*

Great.

John H. Batten, *Chief Executive Officer*

I would add that—with that, though, we are taking—we are gaining market share in Asia and North America, even in a down market. I would expect our growth rate to vet—in (inaudible) to continue to outperform the market growth rate.

Rand Gesing, *Neuberger Berman*

Okay, great. Looking forward to better results in the second half and a brighter '21. Thanks.

John H. Batten, *Chief Executive Officer*

Thanks, Rand. So are we. Thank you.

Operator

Again, if you would like to ask a question, please press star, one at this time. Again, that's star, one to ask a question.

We'll take our next question from Simon Wong with G. Research.

Simon Wong, *G. Research*

Good morning, John and Jeff.

John H. Batten, *Chief Executive Officer*

Good morning, Simon.

Simon Wong, *G. Research*

Can you qualify how big your energy business is this quarter?

John H. Batten, *Chief Executive Officer*

It's a good question. We know specifically that the units that shipped, energy-wise. The aftermarket is a little bit more of a guess. I would say it's in the $5 million to $6 million—around $5 million. It would be my best guess when you combine forward and aftermarket.

Simon Wong, *G. Research*

Okay. There is some new builds in there. I mean …

Jeffrey S. Knutson, *Vice President of Finance, Chief Financial Officer, Treasurer and Secretary*

In Asia.

Simon Wong, *G. Research*

Okay.

John H. Batten, *Chief Executive Officer*

Yes. I would guess, yes. Half that at most—I would say, Simon, 90 per—well, in the second quarter, 100% of the new units went to China.

Simon Wong, *G. Research*

Okay. Okay, great. I'm just trying to understand, how big is the aftermarket business? That's what I was trying to get at, because I (inaudible).

John H. Batten, *Chief Executive Officer*

Aftermarket (inaudible) or after …

Simon Wong, *G. Research*

Aftermarket for the energy business.

John H. Batten, *Chief Executive Officer*

I would say this quarter it was roughly half.

Simon Wong, *G. Research*

Okay. Okay. Then you also have some energy business going to the offshore. I've been hearing that offshore they've been picking up for a few quarters now. Are you seeing that in your order rate, incoming orders, a pickup in offshore?

John H. Batten, *Chief Executive Officer*

We're just starting to see some project quote activity. Fortunately, all of that's being handled by Inventory at our—existing inventory at our distributor. First thing we have to do for us is get inventory that's sitting out into the market, and then we'll get replacement orders. I would say there's been some signs of—some small signs of life in that market.

Simon Wong, *G. Research*

That's encouraging. If I was to look back five or six years ago, how big was this offshore initiative for you?

John H. Batten, *Chief Executive Officer*

Oh, five or six. You're going back to almost our peak …

Simon Wong, *G. Research*

Yes.

John H. Batten, *Chief Executive Officer*

That probably would have been 20—Simon, , I will double check for you. I would imagine $20 million.

Simon Wong, *G. Research*

Okay, all right, great.

John H. Batten, *Chief Executive Officer*

(Inaudible)

Simon Wong, *G. Research*

Then, on the covenant side, you mentioned that you just got an amend equal to four times leverage. How long's that amendment good for and what does it go back after the amendment ends?

Jeffrey S. Knutson, *Vice President of Finance, Chief Financial Officer, Treasurer and Secretary*

Yes. There's an 8-K that will be filed. You can see the details. But essentially we've got a four-to-one for the quarter that just ended. Goes up to five-to-one in the next quarter, and then starts backing down over the next two quarters. Then we get back to the three-to-one in the second quarter of Fiscal '21 or the fourth quarter of calendar '20. It's really three, four quarters of relief.

Simon Wong, *G. Research*

Okay. All right. Great. That's all the questions I have. Thank you.

John H. Batten, *Chief Executive Officer*

I guess the other—Simon, the other component that may be important is we—it also includes the add back of the $3.9 million charge in Q1. If you remember the product performance charge (inaudible) EBITDA, treating that essentially as a restructuring type of charge.

Simon Wong, *G. Research*

Okay, great. Thank you.

John H. Batten, *Chief Executive Officer*

Yes.

Operator

It appears there are no further questions at this time. Mr. Batten, I'll turn the call back to you for any additional or closing remarks.

John H. Batten, *Chief Executive Officer*

All right. Thank you, Christina. Thank you for joining our conference call today. We appreciate your continuing interest in Twin Disc. We hope that we've answered all of your questions. If not, please feel free to call Jeff or myself. We look forward to speaking with you again, probably when we close our fiscal 2020 third quarter.

Christina, now I'll turn the call back to you.

Operator

Thank you. This concludes today's call. Thank you for your participation. You may now disconnect.