Federal Signal Corporation

Third Quarter 2022 Earnings Conference Call

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PRESENTATION

Operator

Good morning, and welcome to the Federal Signal Corporation Third Quarter 2022 Earnings Conference Call.

Please note this even is being recorded.

I would now like to turn the conference over to Ian Hudson, Chief Financial Officer. Please go ahead.

Ian Hudson

Good morning, and welcome to Federal Signal's Third Quarter Conference Call. I'm Ian Hudson, the company's Chief Financial Officer. Also with me on the call today is Jennifer Sherman, our President and Chief Executive Officer. We will refer to some presentation slides today as well as to the earnings news release, which we issued this morning. The slides can be followed online by going to our website, federalsignal.com, clicking on the Investor Call icon and signing into the webcast. We have also posted the slide presentation and the earnings release under the Investor tab on our website.

Before we begin, I'd like to remind you that some of our comments made today may contain forward-looking statements that are subject to the Safe Harbor language found in today's news release and in Federal Signal's filings with the Securities and Exchange Commission. These documents are available on our website. Our presentation also contains some measures that are not in accordance with U.S. generally accepted accounting principles. In our earnings release and filings, we reconcile these non-GAAP measures to GAAP measures. In addition, we will file our Form 10-Q later today.

I'm going to begin today by providing some detail on our third-quarter results before turning the call over to Jennifer to provide an update on our performance, current market conditions, recent acquisition activity, and our outlook for the remainder of the year. After our prepared comments, Jennifer and I will address your questions. Our consolidated third-quarter financial results are provided in today's earnings release. In summary, our businesses were able to deliver another solid quarter with double-digit growth in net sales and earnings, gross margin improvement, and an Adjusted EBITDA margin towards the upper end of our target range.

Consolidated net sales for the quarter were $346 million, up $48 million or 16% compared to last year despite a $3 million unfavorable foreign currency translation impact. Organic revenue growth for the quarter was $27 million or 9%. Consolidated operating income for the quarter was $39.5 million, up $5.2 million or 15% compared to last year. Consolidated Adjusted EBITDA for the quarter was $53.5 million, up $6.1 million or 13% compared to last year. That translates to a margin of 15.4% in Q3 this year compared to 15.9% last year. Net income for the quarter was $31.8 million, up $2.6 million or 9% from last year. That equates to GAAP EPS for the quarter of $0.52 per share, up $0.05 per share or 11% from last year.

On an adjusted basis, EPS for the quarter was $0.53 per share, an improvement of $0.05 per share or 10% compared to last year. Our third quarter GAAP and adjusted EPS in both the current and prior year included certain discrete tax benefits, primarily related to tax planning strategies. In the current year quarter, these benefits totaled $3.8 million, which was $700,000 less than the amount recognized in the prior year quarter. Order intake for the quarter was again strong with orders of $382 million, representing an increase of $32 million or 9% compared to Q3 last year. Consolidated backlog at the end of the quarter set another new company record at $824 million. That represents an increase of $337 million or 69% from last year.

In terms of our group results, ESG's net sales for the quarter were $285 million, an increase of $36 million or 14% compared to last year. ESG's operating income for the quarter was $33.9 million, up $3.1 million or 10% compared to last year. ESG's Adjusted EBITDA for the quarter was $46.5 million, up $3.8 million or 9% compared to last year. That translates to an Adjusted EBITDA margin of 16.3% in Q3 this year compared to 17.1% last year. ESG reported total orders of $321 million in Q3 this year, an improvement of $29 million or 10% compared to last year.

SSG's net sales for the quarter were $62 million, up $12 million or 25% compared to last year. SSG's operating income for the quarter was $10.5 million, up $2.9 million or 38% from last year. SSG's Adjusted EBITDA for the quarter was $11.5 million, up $3 million or 35% from last year. SSG's Adjusted EBITDA margin for the quarter was 18.7%, up 140 basis points from Q3 last year. SSG's orders for the quarter were $61 million, up $2 million or 4% compared to last year. Corporate operating expenses for the quarter were $4.9 million compared to $4.1 million last year.

Turning now to the consolidated income statement, where the increase in sales contributed to an $11.9 million improvement in gross profit. Consolidated gross margin for the quarter was 23.9%, up 10 basis points compared to last year. As a percentage of sales, our selling, engineering, general and administrative expenses for the quarter were up 30 basis points from Q3 last year. Other items affecting the quarterly results include a $300,000 increase in amortization expense, a $400,000 reduction in other income and a $1.6 million increase in interest expense. Tax expense for the quarter was $4.9 million compared to $4.3 million last year, with the increase primarily due to the recognition of fewer discrete tax benefits in the current year quarter compared to the prior year. Our effective tax rate for the quarter was

13.4% compared to 12.8% last year. At this time, we expect our full-year effective tax rate to be approximately 22%.

On an overall GAAP basis, we, therefore, earned $0.52 per share in Q3 this year compared with $0.47 per share in Q3 last year. To facilitate earnings comparisons, we typically adjust our GAAP earnings per share for unusual items recorded in the current or prior quarters. In the current year quarter, we made adjustments to GAAP earnings per share to exclude acquisition-related expenses. On this basis, our adjusted earnings for the quarter were $0.53 per share compared with $0.48 per share last year. Looking now at cash flow, where we generated $10 million of cash from operations during the quarter, bringing the total year-to-date operating cash generation to $32 million. We ended the quarter with $296 million of net debt and availability under our prior credit facility of $160 million.

We recently increased our borrowing capacity by executing a new 5-year $800 million credit facility, replacing the $500 million credit facility that was previously in place. The new credit facility provides greater financial flexibility to invest in internal growth initiatives and pursue additional strategic acquisitions like TowHaul Corporation, which we acquired shortly after the end of the quarter for an initial payment of $43 million. The terms of the new facility are more favorable to the Company, reflecting our strong cash flow and balance sheet. This marks another important milestone for the Company as we continue to execute on our strategic long-term growth objectives. We also remain committed to investing in organic growth initiatives and returning cash to stockholders through dividends and opportunistic share repurchases. On that note, we paid dividends of $5.5 million during the quarter, reflecting a dividend of $0.09 per share, and we recently announced a similar dividend for the fourth quarter.

That concludes my comments, and I would now like to turn the call over to Jennifer.

Jennifer Sherman

Thank you, Ian. With benefits from pricing actions, strong aftermarket demand and contributions from recent acquisitions, our businesses were able to deliver double-digit year-over-year net sales and earnings growth, gross margin improvement, and an EBITDA margin towards the high end of our target range despite supply chain disruption, which impacted production and shipments at certain facilities within our Environmental Solutions Group early in the quarter. Within our Environmental Solutions group, we again saw increased demand for rentals, parts and used equipment, driven in part by the extended lead times for new equipment. Overall, our aftermarket revenues in Q3 this year were up 10% over last year, with particularly strong demand for rentals and parts sales.

The growth of our aftermarkets business remains a key strategic initiative and with benefits from pricing actions, geographic expansion into new territories, and acquisitions leveraging our aftermarkets platform, we were pleased to report our highest aftermarket revenues in any third quarter. In total, aftermarket revenues represented about 30% of ESG's revenues for the quarter. The volatile supply chain environment in which we are currently operating is causing us to constantly adjust our production schedules, creating a high degree of inefficiency and impacting our ability to ship units. During the quarter, production shipments at our Streator and Elgin manufacturing facilities were adversely impacted by supply chain disruptions, primarily related to sporadic shortages in hydraulics and specialty control components.

We are partially building trucks and completing them when the missing parts arrive. For example, in July, 30% of the units scheduled to be built at our Streator facility were waiting for parts at the end of the month. In response, the teams worked diligently to secure additional parts as well as to qualify alternative suppliers. The encouraging news is that as the quarter progressed, we saw sequential monthly improvement in production. In fact, September represented our highest weekly unit production at both facilities this year with build rates up 35% since January. Street Sweeper production also experienced a planned temporary decline in July as our LGIM facility implemented a lean manufacturing initiative to reconfigure one of its production lines. While the assembly line reconfiguration had a temporary impact in July, production ramped back up in August and September. Towards the end of the quarter, we also experienced some customer pickup delays resulting from Hurricane Ian, particularly in our dump body business. We are fortunate that our facilities and employees were not directly impacted by this extreme weather event and are pleased that our equipment is playing a critical role in repairing and rebuilding the damage to housing and infrastructure in the affected areas.

Within our Safety and Security Systems Group, the supply chain improvement we started to see towards the end of last quarter continued into the third quarter. Over the course of the last several months, our procurement and engineering teams have worked diligently to add alternative suppliers for various components like LEDs and wire harnesses and have redesigned printed circuit boards to replace unavailable, obsolete or long lead time electronic components. We have also brought certain production in-house to alleviate some pressure on our key suppliers. For example, we have added in-house capacity to offset demand shortages from our contract manufacturer for printed circuit boards that are used in our past finder products.

With these affords gaining traction, we saw an improvement in inventory availability. The supply chain became more reliable as the quarter progressed, and our operations team put together a robust execution plan to build out the increasing backlog by flexing the workforce, working overtime and hiring additional resources. These factors contributed to SSG's record third-quarter performance, which included 25% top-line growth at an EBITDA margin in excess of its target range. I'll conclude my comments on Q3 by reiterating that while supply chain remains burdensome, we have seen improvement within SSG and are encouraged by the recent improvement in production levels that we've seen in our Streator and Elgin facilities.

During the quarter, as production levels increased, we saw sequential monthly improvement in sales, and despite the volatile supply chain environment we have been operating in so far this year, we remain on track to have a record year in terms of sales and earnings. Demand for our product offering continues to be as strong as ever as demonstrated by our outstanding third-quarter order intake of $380 million, contributing to another record backlog and reflecting strength across our end markets.

This sentiment has been widely shared by our customers and dealer partners and seems to be further solidified by the economic stimulus package, which passed in March of 2021. In that package, approximately $350 billion was earmarked for state, local and territorial governments for a variety of purposes, including the maintenance of essential infrastructure such as sewer systems and streets. As a provider of equipment used for essential services, like Steward Cleaning & Street sweeping, we stand a benefit meaningfully from additional aid that may be provided to state and local sources for these purposes. The treasury began distribution of the first $175 billion tranche in the spring of 2021 and current indications are that the second tranche is expected to be released this year.

The dealer sentiment remains bullish as municipalities, both small and large, are continuing to place orders at historic levels based in part by a surplus of funds directly attributed to this public funding source. This is supported by the ongoing strength of U.S. municipal orders, which were up 20% for both the quarter and year-to-date period with notably strong demand for street sweepers and sewer cleaners. In fact, so far this year, our U.S. municipal orders for street sweepers are up around $40 million or 40% over last year, while sewer cleaning orders are up $25 million or 22% over the same period. We are also seeing strong domestic municipal demand within SSG with 9% order improvement year-to-date, resulting from higher demand for public safety equipment.

Over the last few years, several major urban domestic municipalities have paused making investments in public safety equipment such as police vehicles and related equipment. We are pleased that this trend appears to just started to reverse. During Q3, we received a significant order from a major metropolitan police department, the first in over three years, and we are optimistic that other customers will follow with renewed investment in public safety equipment. Within our industrial end markets, we've also seen a 15% year-over-year improvement in domestic orders.

The improvement has been almost across the board, but most notably for our TRUVAC safe digging trucks and our Guzzler industrial vacuum loaders, which collectively were up $41 million or 66% year-over-year. While industrial order strength continues, we have seen some softening in orders for dump bodies as customer and dealer-provided stock chassis and pool chassis of all size classes remain a primary constraint for this product offering as dump bodies typically receive lower prioritization from dealers when chassis availability is limited based on allocations from OEMs. As chassis availability improves, we expect to see increased orders based on pent-up demand.

Turning to the $1.2 trillion infrastructure bill, which has $550 billion for new investments in roads, bridges, power, water and broadband infrastructure, public transportation, and airports, we are beginning to see demand pick up in the form of equipment inquiries from contractors who are working with state department of transportation agencies on roads, bridges, and related projects. Additionally, conversations among our dealer channel indicate contractors are now planning out projects through 2024 and are beginning to commence with large equipment inquiries directly tied to these infrastructure funds.

I would now like to spend a minute on our acquisition of TowHaul which we completed in early October. TowHaul is headquartered in Belgrade Montana and is a leading manufacturer of off-road towing and hauling equipment. For over four years, TowHaul has been dedicated to designing and manufacturing the most reliable and efficient, and adaptable heavy-duty off-road specialty extraction support equipment, including its signature front-end and rear loading load boy trailers. TowHaul's patent equipment designs, depth of product knowledge, understanding of its customer-specific requirements and excellent track record have allowed us to establish a leading position in the industry. TowHaul also supports the recurring aftermarket needs of its customers through parts and service offerings, which represent approximately 35% of its annual revenue. The acquisition further bolsters our position as an industry-leading diversified industrial manufacturer of specialty vehicles for maintenance and infrastructure markets with leading brands of premium value-adding products and a strong supporting aftermarket platform.

The combination of TowHaul with Ground Force Worldwide, which we acquired in October of last year, allows us to serve our shared global customer base with a broader range of world-class products and solutions. It also creates a platform that is well-positioned to capitalize on a number of tailwinds expected to drive future growth in the metal extraction industry, including robust industrial activity and increased demand for precious metals in support of vehicle electrification and other green initiatives.

Last year, TowHaul generated revenues of approximately $23 million, we expect that TowHaul will be able to perform within ESG's target EBITDA margin range and will be accretive to earnings in 2023. The acquisition reiterates our expectation that M&A will continue to contribute meaningfully to our future growth.

Turning now to our outlook for the rest of the year. Overall, demand for our products and our aftermarket offerings remains high with our third-quarter orders up 9% year-over-year and our backlog at the end of the quarter, again, setting a new company record. Although we expect sporadic supply chain disruption to continue in some manner for the next several quarters, our teams continue to respond to these challenges, and we are encouraged with the recent improvement we have seen. With our performance so far this year, our record backlog, and current expectations of component availability, we are raising the midpoint of our full-year adjusted EPS outlook by establishing a new range of $1.91 to $2, updated from the previous range of $1.85 to $2. We are also raising the midpoint of our full-year net sales outlook to a new range of $1.41 billion to $1.44 billion, updated from the previous range of $1.38 billion to $1.45 billion.

We remain encouraged by the long-term opportunities for all of our businesses, which will further benefit from the bipartisan infrastructure legislation passed by Congress. We are already starting to see the benefits from the economic stimulus packages, which started to be made available to municipalities earlier this year, and we also expect the infrastructure bill with $550 billion in new spending, we could see capital equipment demand increase to support infrastructure investments in areas such as roads, bridges, electrification, broadband, clean energy and water and public transportation buildup. We are a leading manufacturer of specialty infrastructure and maintenance equipment and anticipate increased demand for the majority of our product offerings, including equipment sales and rentals of dump truck and trailers, safe-digging trucks, road mark equipment, sewer cleaners, and street sweepers. We expect to see a prolonged meaningful tailwind from these stimulus packages.

With our strong demand and record backlog, we are not currently seeing any leading indicators of a recession. Our pricing actions have been generally accepted in the market, and we have not experienced any meaningful order cancellation activity. In fact, in our businesses, order cancellations have been rare. Further, while no company is immune to a macroeconomic recession, our backlog provides us with good visibility into 2023 and in part, insulates the Company from the more immediate effects of an economic slowdown. Over the last several years, we have transformed our end market exposure and implemented a revenue diversification strategy that has enabled us to adjust as needed to market conditions. With that in an ongoing focus on ETI principles, Federal Signal has become a more resilient business, delivering a consistent level of EBITDA margin above most of our peers. As Ian noted in his comments, our financial position and liquidity are strong and the recent expansion of our credit facility will further enable us to pursue strategic acquisitions like TowHaul.

Our current M&A pipeline continues to be very active. We remain committed to our vehicle electrification initiatives, including incorporating weeks and acquisitions into our electrification roadmap. For example, the Switch and Go product line, which was part of the Dice acquisition last December, has entered into an agreement with an EV chassis manufacturer to build a prototype vehicle with the switch and go body system. The value proposition maximizes the benefits of the EV chassis by offering multiuse body system capabilities that is not possible with a standard fixed body application.

In simple terms, Switch and Go's interchangeable body solution enables an end user to use one vehicle to the work of two to three trucks. We also continue to experience a high level of demand from our dealer network for demonstrations of our plug-in hybrid electric street sweeper products, specifically the Broom Bear and the 3-wheel Pelican and have received additional order intake. Our ongoing commitment to environmental, social, and governance initiatives also position us well in the communities in which we operate and is a differentiating factor in our ability to attract labor at most of our facilities.

As an example, at our Streator facility, where we produce Vector, TRUVAC and user equipment, we currently have less than 20 hourly job openings, which is less than 4% of the workforce. Our access to high-quality employees continues to benefit from our deep roots in the Streator community. For example, we've been able to successfully hire welders from our partnership with the local community college. In October, we held an open house of the facility that was attended by over 1,400 employees and family members, which is a further testament to the strong bond the team has built for its employees in the local community.

We're also thrilled to report that our chat stream business was recently recognized as a top place to work in Houston for the second year in a row. We recently held our annual leadership off-site meeting, which was attended by over 60 executives. At this event, our leadership team engaged a series of interactive sessions covering macroeconomic topics such as the state of the economy, DE&I initiatives and a futuristic workshop as well as sessions focused more specifically on our strategic initiatives. We enjoyed welcoming leaders from recently acquired companies.

This event always reminds me of how proud I am of the culture we've developed at Federal Signal, and I feel fortunate to work with so many talented leaders. We all left the event feeling energized and excited about our future. Although we've been operating in a difficult supply chain environment for over a year, we believe that the mitigating actions we have taken in response will provide longer-term benefits to Federal Signal, and we will emerge a stronger company.

We recently reorganized our supply chain group to improve material availability across the organization and drive cost-reduction initiatives as we leverage our scale and integrate acquired companies. In addition, we've expanded both our external supply base and our in-sourcing capabilities. For example, we are now producing parts at certain FS solution centers that are utilized by our dump body business and our SSG and ESG team successfully collaborated to reengineer certain equipment in response to electrical component shortages. We have also invested in inventory, securing safety stock to support production as we work towards reducing our current lead times. With strong demand and ongoing tailwinds from infrastructure stimulus, our good access to labor and recent capacity expansions, we are well positioned for growth as the supply chain environment continues to improve.

At this time, I think we are ready for questions. Operator?

Operator

Thank you very much.

The first question comes from Steve Barger from KeyBanc Capital Markets. Please go ahead.

Steve Barger

Thanks. Good morning. Your updated guidance implies a record 4Q revenue performance. Is that coming more from the line side to already build product that you can ship on top of plan production? Or do you just expect fewer constraints in 4Q?

Ian Hudson

Yes. I think, Steve, what we've seen in the last couple of months, certainly of Q3 with the improvement in production. We're expecting some of that to continue. Now we have some seasonality there where aftermarket tends to taper off a little bit. But, I think the combination of the size of our backlog and the production improvements we've seen in the recent months gives us confidence that the revenue will certainly be up over Q3. So, that's what's implied in the outlook.

Jennifer Sherman

Also, we expect our margins in Q4 to be up year-over-year.

Ian Hudson

Yes. I guess to that point, ESG incremental margin has obviously been tough for the last five quarters. I know a big driver of that is all the operational challenge that you discussed. I just want to gauge your confidence that nothing has really changed on your ability to convert higher sales to higher margin as you get past some of these supply chain constraints.

Jennifer Sherman

Yes. The most encouraging fact that I saw is we track pretty carefully our production levels at Elgin and Vector. As I talked about in my prepared remarks, as we move through July, August, and September, we saw a sequential improvement each month. In September, we were up 35% over January. So although there's still some pockets of supply chain, overall, we're moving in the right direction, and we're encouraged by that, and that was baked into the guidance.

Steve Barger

Yes. In an unconstrained environment, how much of the $765 million of ESG backlog is shippable in 2023?

Ian Hudson

All of it would be, yes.

Jennifer Sherman

All of it.

Steve Barger

So nothing scheduled for '24. That all represents orders that people want right now, if they could get it.

Ian Hudson

Correct.

Jennifer Sherman

Correct.

Steve Barger

I think I've asked this before, but just to remind us, given the capacity expansions, what do you think quarterly revenue capacity is at ESG? Again, unconstrained.

Ian Hudson

I think unconstrained, Steve, I think we've obviously added a couple of companies into the mix over the last couple of years. But I think unconstrained, I think if you looked at some of our order cadence within SSG, it's certainly been in the $300 million, if not in excess of the $300 million range. So I think north of $300 million plus the impact of acquisitions.

Steve Barger

Okay, that's perfect. Thanks. I'll get back in line.

Jennifer Sherman

Thank you.

Operator

Thank you. The next question comes from Mike Shlisky from D.A. Davidson & Company. Please proceed.

Michael Shlisky

Yes hey good morning. Thanks for taking question. Can you hear me okay?

Jennifer Sherman

Yes.

Michael Shlisky

Great. Can I first touch on the new facility that you've got out there? Can you just give us a couple of points as to some of the changes that might be in terms as far as the spread or any ticking fees or other fees that may be involved, just eking (phon) out our model properly calibrated here?

Ian Hudson

Yes. So, no real change in the terms in terms of pricing, Mike. It's very similar spreads that were in the prior agreement. Now obviously, we've switched from LIBOR to the new sulfur rate. And so, with the increase in rates, the interest expense is going to be higher. But in terms of the other terms of the agreement that changed, there's some more favorable terms in terms of the covenant calculations that benefit us. Obviously, there is the increase in the overall size of the facility. There's also the ability to increase it further for acquisitions, if that need arises. So, I think overall, we had the credit agreement that we previously had was going to expire in 2024. We thought it was an opportunistic time to look to refinance it for another five years and also increase the facility. So, we're really pleased with the outcome.

Jennifer Sherman

Obviously had one thing to reiterate what Ian said, in these challenging credit markets, we were extremely pleased with the response that we got and the terms that we got. We feel like it well positions us going forward in terms of optionality for both organic growth and inorganic growth.

Michael Shlisky

Excellent. Jennifer, I wanted to just get some more color from you on those, the dump body order comments you made during your prepared remarks. I wasn't sure I quite followed it. Did you say that dump bodies get a little bit lower priority in times of chassis shortages and that seems in a somewhat new comment? Is that a new development in the industry? Or, is that the way it's always been, we just haven't heard about it since?

Jennifer Sherman

Yes. No. That's the way it's always been. And when chassis are on allocation, many dealers won't want to commit to necessarily dump truck fleet. They want to keep their options open. So we've seen some of that over the last several quarters. As we move forward, we believe that a couple of things, one, there's pent-up demand. Number two is we've diversified the end markets of that business pretty significantly since we purchased TBI in 2017. OSW Switch & Go both have strong municipal exposures. So we'll start to see the benefits of that. And then infrastructure bill, it's very difficult to imagine an infrastructure project that doesn't need a dump body. So, as we move forward, we're encouraged by the opportunity, particularly around the infrastructure funds and we wanted to just point out in perhaps a clearer way. one of the drivers of the softness in orders is just the prioritization of dump truck in the queue for chassis.

Michael Shlisky

Okay. That's great color Jennifer. Thank you. I'll pass it along.

Operator

Thank you. The next question comes from Chris Moore from CJS Securities. Please go ahead.

Christopher Moore

Good morning. Yes, maybe just back to the September highest production rates this year. Was that follow-up? And, how did it look in October?

Jennifer Sherman

Yes, we're still getting our October 1st. So, more to come on that. But overall, we saw the beginnings of supply chain improvement at our SSG group in Q2 and that continued in Q3 for SSG. As we move through the quarter, at specifically our Streator and Elgin facilities, we saw that improvement, and we are encouraged. The other thing that's happening, and this will have a long-term benefit for the Company is we've now qualified additional suppliers. We've streamlined some of our product offerings as a result of the supply chain challenges. So, we've become much more nimble in terms of responding to this. I believe that we will be in a better position longer term as a result of it.

Christopher Moore

Got it. Very helpful. Just with respect to the adjusted EPS range. The tax rate is 22%. Is that a lower tax rate assumption after Q2 or the same?

Ian Hudson

It is, Chris, because I think we talked about the discrete benefits that we had in Q3. So, it is slightly lower than what we've previously signaled in Q2, but 22% would be the full-year effective rate that we're expecting.

Christopher Moore

Got it. That wouldn't necessarily be a new normalized level moving forward to just for 22 (phon)…

Ian Hudson

Sorry, Chris. Not necessarily. No, that 22% would include the discrete benefits we recognized in Q3, which I think we talked about on the prepared remarks that we also had some fairly significant discrete benefits in Q3 last year. So, when you look at it year-over-year in Q3, I think our effective rate was at a fairly similar level, 13% this year. I think it was a high 12s last year. So, we had a fairly similar amount of discrete benefits in Q3 of both periods. But the 22% for the full year would include the impact of the discrete benefits in the third quarter.

Christopher Moore

Got it. I appreciate that. Just from a volume price discussion, the midpoint of current revenue guidance, 17.5%, something like that, what's the rough split between volume and price?

Ian Hudson

Yes. It's probably in terms of the organic growth, if you look at Q3, we had organic growth was about $27 million, about 9%, and of that, about half of it was pricing. So, we would expect similar dynamics, I think, entering the fourth quarter.

Christopher Moore

Got it. All right. Appreciate it. I will leave it there.

Ian Hudson

You're welcome.

Operator

Thank you. The next question comes from Greg Burns from Sidoti Income. Please proceed.

Gregory Burns

Is there any way you could quantify how much revenue the disruptions in the ESG side of the business cost…

Operator

Sorry to interrupt you. The audio is not clear from your line. Please use the handset mode.

Gregory Burns

Okay. Do you hear me now?

Jennifer Sherman

We heard you.

Gregory Burns

Okay. Yes. So, is there any way you could quantify how much the disruptions cost you in terms of revenue and margin this quarter?

Ian Hudson

It's a little tough to quantify and pinpoint an exact number, Greg, because it had some knock-on effect because as we talked about in July, we were impacted more than in August and September. So there is some catch-up effect that we had. But, if I were to ballpark an estimate, we're talking $20 million-ish would be a high-level estimate, but as I said, it's a fairly difficult number to pinpoint.

Gregory Burns

Okay. Then with the TowHaul acquisition, is ground force a reseller of TowHaul? Like how much revenue does Ground Force account for TowHaul or is that not a meaningful number? And, is there any additional revenue synergies between the two acquisitions?

Ian Hudson

Yes. It's not so much a reseller, but what they can do, and this is where we see some opportunities, they can go to market together. There is situations where Ground Force has a strong presence in a certain geographic market where TowHaul doesn't necessarily have a strong presence, and it also works vice versa. So, I think the combination of the two teams can attack all of the geographic markets in which they operate. So, I think that's where we see a nice opportunity from a synergy standpoint. In terms of the TowHaul deal, we're targeting synergies of around about $3 million by the end of year three. The majority of those are revenue synergies from leveraging both the distribution channels.

Gregory Burns

Okay. Great. Thank you.

Operator

Thank you. The next question comes from Walt Liptak from Seaport. Please go head.

Walter Liptak

Hi good morning. Congratulations on the good quarter. I've got a couple of follow-ons for you. First on the TowHaul. I think in your prepared remarks, you talked about TowHaul as a platform, and I assume that's with Ground Force. I wonder if you could talk about that? Are there other M&A deals that you're looking at in this metal distractions or middle distraction space? Thank you.

Jennifer Sherman

Yes. So, Ground Force and TowHaul sell to the same customers, and they support the equipment that's in the mine. So, they basically transport to and from the mine is a way to think about it. They're the leading providers in the world. TowHaul has certain geographic areas that it focuses on. Ground Force doesn't and Ground Force is focused on certain areas and certain customers that TowHaul is not. So, we're very excited about putting the two together under the same management team, leveraging the same sales channel because as we mentioned, we think there's synergies there. There could be one more deal that completes that platform.

But we're still right now very focused on integrating the two companies that we purchased. But as we previously talked about, Ground Force is off to a strong start. Both of those companies operate within our target EBITDA margin ranges. There's opportunity for improvement. So, very solid businesses. And what we really like about them also is their parts business. We talked about TowHaul has 30% plus parts business, and so as we move forward, it does a really nice job with some proprietary parts in this particular market.

Walter Liptak

Okay. Great. Then switching gears to another follow-on. It's great to see that the supply chain started to improve production levels are getting better. Sort of a follow-on to that last question about delayed shipments. I wonder if you can quantify it a different way, what are your lead times now in terms of months or whatever? In normal times, where were those lead times? How supply chains get better, how quickly could you work down that ESG backlog?

Jennifer Sherman

Yes. So, for several of our product lines, I'll start with they're too long, and we have very focused efforts to reduce those lead times. Particularly Vector, we've seen very strong orders for many of our products, including our Vector and Elgin products. So, that's an area where we will be focused on reducing those lead times moving forward. Particularly, we're encouraged by because we've got the capacity, and we've got the people, and so as we move forward, we should easily be able to reduce lead times, and we should be able to increase throughput.

Walter Liptak

Okay. Fair enough. And then just a new question, I guess, is that we're in this rising interest rate environment, it's right that you've got all the government spending for infrastructure and other things. But how do you think the rising interest environment impacts your customers' purchases of your products?

Jennifer Sherman

Yes. So, on the municipal side of things, we don't see a big impact. Particularly as you know, sewer cleaners are often funded by water taxes, and then we have the multiple layers of government spending that will benefit purchases of our products. On the industrial side of things, that's where we believe our aftermarkets business is so important because we have rentals as an option. Because as I mentioned in my prepared remarks, we are starting to—our customers are starting to plan for some of these big infrastructure projects. So, we have programs that are available through our aftermarkets group if they can't afford to buy new equipment where they can rent equipment and buy it over time, if necessary. So we think we're uniquely positioned because of our ability to offer both new, used and rental equipment in this rising interest rate environment.

Walter Liptak

Okay. Great. All right. Thank you.

Operator

Thank you. The next question comes from Felix Boeschen from Raymond James. Please go ahead.

Jennifer Sherman

Good morning Felix.

Ian Hudson

Good morning.

Felix Boeschen

Ian, I was hoping just to follow up on something real quick, and I'm not sure if I missed it, but can you provide how much chassis pass-through revenue was in the quarter and how that compares to last year?

Ian Hudson

Yes, it was a little higher. It was about 6 million higher. So, it was about 1% of the overall revenue increase was higher chassis revenue. It was about a drag on our margin of around about 15 basis points this period. So, not as much of a drag as it was in Q2, but still a slight drag on gross margin.

Felix Boeschen

Okay. Super helpful. Then I wanted to follow up on the September build rate commentary being the highest of the year. I think you said up 35% versus January. I think there was a comment across both Vector and Elgin. A, I was hoping a, could you confirm that it was across both of those? And then b, any idea or any color for us how volumes at this point compared to sort of pre-COVID, pre-after expansion levels?

Jennifer Sherman

Yes. So I will confirm, yes, it was for Vector and out for Streator Elgin. Number two is with respect to pre-COVID levels, we're not there.

Felix Boeschen

Okay. Still lower than pre-COVID.

Ian Hudson

Yes.

Felix Boeschen

Okay. Then just my last one. I understand you're not giving guidance for 2023. But I am kind of curious if you could directionally talk about maybe what you're hearing out of the OEMs on chassis allocation into next year. Any directional color on maybe how you're thinking about that specifically in the municipal part of your book?

Jennifer Sherman

Sure. So, we received initial allocations from the chassis OEMs, and the messaging is about the same as 2022 with potential upside for the second half of the year. However, all that being said, as we've talked about several times, we have programs in place with our dealers where we encourage them to go out and secure chassis outside of our allocations. And then in addition to that, we also go out and try to secure chassis. We call it the onesie-twosie program for various distributors across North America. I know we've started that. So, as we move into '23, we have several programs in place where we're trying to increase the number of chassis that are available to us, either through our dealers, our customers, or going out and trying to procure them on an individual basis.

Felix Boeschen

Got. Very helpful. I'll stop there.

Jennifer Sherman

Thank you.

Operator

Thank you. The next question comes from Steve Barger from KeyBanc Capital Markets. Please go ahead.

Steve Barger

Hey thanks. Just a quick follow-up. Sorry if I missed this. Operating cash flow is running below prior year. I know 4Q is typically a cash release period. Do you have a forecast for operating cash flow for either 4Q or the year?

Ian Hudson

We don't have a forecast necessarily, Steve. But I think one thing we would say is that we would expect our cash conversion in Q4, obviously, to improve from where it's been. I think as you can probably see, we've had some strategic inventory build really to serve the backlog that we have. There is some, obviously, increase in our receivables that is primarily timing related. I think we started to see some of that turn in the early part of October. The encouraging thing that we see in terms of our receivables is that we haven't seen any deterioration in terms of the aging profile of our receivables, even though it's up significantly at the end of September versus where it was at the end of December. So, I think the receivables will start to turn as we enter Q4, and that's where we're expecting to see some of the cash conversions start to improve in Q4.

Steve Barger

Got it. That's perfect. Thanks.

Jennifer Sherman

Thank you.

Operator

Thank you. This concludes our question-and-answer session. I would like to turn the conference back over to Jennifer Sherman for closing remarks.

Jennifer Sherman

Thank you. In closing, I would like to reiterate that we are confident in the long-term opportunities for our businesses and the prospects for our recent acquisitions. Our portfolio of businesses include many market-leading brands with solid fundamentals. Our foundation is strong, and we are focused on delivering profitable long-term growth through the execution of our strategic initiatives. I'd like to give a public thank you to all of our employees for their commitment, creativity and dedication addressing this challenging supply chain environment. I would also like to express our thanks to our stockholders, distributors, dealers and customers for their continued support. Thank you for joining us today, and we'll talk to you soon.

Operator

Thank you. The conference has now concluded. Thank you for attending today's presentation. You may now disconnect your lines.