



Federal Signal Corporation
First Quarter Earnings Conference Call
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CORPORATE PARTICIPANTS

Ian Hudson, *Chief Financial Officer*

Jennifer L. Sherman, *President and Chief Executive Officer*

CONFERENCE CALL PARTICIPANTS

Kenneth Newman, *KeyBanc Capital Markets*

Felix Boeschen, *Raymond James*

Michael Shlisky, *D.A. Davidson*

Daniel Moore, *CJS Securities*

Gregory Burns, *Sidoti & Company*

Walter Liptak, *Seaport Global Securities*

PRESENTATION

Operator

Welcome to the Federal Signal Corporation First Quarter 2022 Earnings Conference Call. As a reminder, all participants are in listen-only mode and the conference is being recorded. After the presentation, there will be an opportunity to ask questions.

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 first 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 first quarter results before turning the call over to Jennifer to provide her perspective on our performance, market conditions, and our outlook for the remainder of the year. After our prepared comments, Jennifer and I will address your questions.

Our consolidated first quarter financial results are provided in today's earnings release. In summary, we delivered solid financial results for the quarter, with 18% top line growth and EBITDA margin performance within our target range, despite a slow start to the year. Consolidated net sales for the quarter were \$330 million, up \$51 million or 18% compared to last year. Consolidated operating income for the quarter was \$28.5 million, up \$700,000 or 3% compared to last year.

Consolidated Adjusted EBITDA for the quarter was \$42.2 million, up \$1 million or 2% compared to last year. That translates to a margin of 12.8% in Q1 this year, compared to 14.8% last year.

GAAP EPS for the quarter was \$0.33 per share, compared to \$0.36 per share last year. On an adjusted basis, EPS for the quarter was \$0.34 per share, compared to \$0.38 per share last year.

Order intake for the quarter was again outstanding, and we again reported record orders in the first quarter, surpassing the previous high which we set in Q4 last year. In total, orders in Q1 this year were \$453 million, an increase of \$69 million or 18% compared to Q1 last year.

Backlog at the end of the quarter was \$751 million, another all-time high for the Company and an increase of \$342 million or 83% compared to Q1 last year.

In terms of our group results, ESG's net sales for the quarter were \$274 million, up \$46 million or 20% compared to last year. ESG's operating income for the quarter was \$26.8 million, compared to \$27.1 million last year. ESG's Adjusted EBITDA for the quarter was \$39.3 million, in line with the prior year. That translates to an Adjusted EBITDA margin for the quarter of 14.3%, compared to 17.2% last year. ESG reported total orders of \$388 million in Q1 this year, an improvement of \$63 million or 20% compared to last year.

SSG's net sales for the quarter were \$56 million, up \$5 million or 10% from last year. SSG's operating income for the quarter was \$7.9 million, up \$700,000 or 10% compared to last year. SSG's Adjusted EBITDA for the quarter was \$8.9 million (audio interference) or 9%. That translates to an Adjusted EBITDA margin for the quarter of 15.9%, compared to 16.2% last year. SSG's orders for the quarter were \$65 million, up \$5 million or 9% compared to last year.

Corporate operating expenses for the quarter were \$6.2 million, down \$300,000 or 5% compared to last year. The reduction was largely due to favorable mark-to-market adjustments of post-retirement reserves.

Turning now to the consolidated income statement, where the increase in sales contributed to a \$6.9 million improvement in gross profit. Including the effects of production inefficiencies that we encountered in the early part of the year, consolidated gross margin for the quarter was 22.9%, compared to 24.7% last year.

On a year-over-year basis, our pricing actions largely covered our cost increases in Q1 (audio interference) dollars. As we had anticipated, this cost inflation did create some margin pressure in Q1; but with the actions we have taken, we are expecting more price realization and margin improvement as we move forward.

As a percentage of sales, our selling, engineering, general and administrative expenses for the quarter were down 50 basis points from Q1 last year.

Other items affecting the quarterly results include a \$700,000 increase in amortization expense and a \$200,000 increase in interest expense.

Tax expense for the quarter was up \$2.1 million, largely due to the recognition of \$1.9 million fewer excess tax benefits from stock compensation activity as compared to last year. As a result, our effective tax rate for the quarter was 25.7%, compared to 18.4% last year. At this time, we continue to expect our full year effective tax rate to be approximately 25%.

On an overall GAAP basis, we therefore earned \$0.33 per share in Q1 this year, compared with \$0.36 per share in Q1 last year. To facilitate earnings comparisons, we typically adjust our GAAP earnings per share for unusual items recorded in the current or prior year 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 \$0.34 per share, compared with \$0.38 per share last year.

Looking now at cash flow, where we generated \$7 million of cash from operations during the quarter. We ended the quarter with \$291 million of net debt and availability under our credit facility of \$162 million. Our current net debt leverage remains low, even after the funding of the purchase of our University Park facility during the quarter for approximately \$28 million. With our financial position remaining strong, we have significant flexibility to invest in organic growth initiatives, pursue strategic acquisitions, and return 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 second quarter. We also funded \$13.6 million of share repurchases during the quarter.

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

Jennifer L. Sherman

Thank you Ian.

During the quarter, our businesses worked diligently to mitigate the impact of ongoing supply chain volatility and increased coronavirus-related disruption that we experienced at many of our facilities in January. As we mentioned on our last earnings call, we were hit particularly hard by an escalation of COVID-related absences in January at essentially all of our facilities. Overall, we estimate that we lost approximately 20,000 direct labor hours across our facilities in January alone. Thankfully, we saw a dramatic reduction in cases in February, which continued into March. After a slow start, we also noted improvement in chassis deliveries within our dump truck business in March. These factors contributed to a meaningful improvement in production levels and customer deliveries as the quarter progressed.

Overall, our top line increased by over \$50 million year over year, with both of our groups reporting double-digit revenue growth, including benefits from pricing actions and contributions from recent acquisitions. Within our Environmental Solutions Group, the 20% year-over-year sales increase was partially driven by higher sales of safe digging trucks, dump bodies, metal extraction support equipment, and trailers.

Our strategy to diversify our revenue streams by broadening our aftermarket offerings also continued to provide benefits in the first quarter. With tightness in the supply chain and extended lead times for new equipment deliveries, we again saw increased demand for rentals, parts, and used equipment sales. Overall, aftermarket revenues for the quarter were up 20% compared to last year, representing approximately \$12 million of ESG's year-over-year revenue growth. We continue to be encouraged by the resilience and growth opportunities of our aftermarket group.

Within our Safety and Security Systems Group, the 10% sales improvement was primarily due to higher sales of public safety equipment. With our efforts to expand our supply base and execution of our ETI principles to insource production of certain materials, component availability for these products has improved in recent months, which resulted in an increase in shipments compared to last year.

Despite the challenges we faced during the quarter, our teams were successful in delivering a consolidated EBITDA margin within our target range. Consistent performance within our target range is a key focus of ours, and we continue to believe this level of sustained operational excellence differentiates Federal Signal from many of our specialty vehicle peers.

Demand for our products and our aftermarket offerings remains at unprecedented levels. The momentum has been across the board, with orders from both municipal and industrial customers up around 25% year over year. Within our municipal markets, we are seeing the benefits from the American Rescue Plan Act, which in 2021 earmarked \$350 billion for state, local and territorial governments for a variety of purposes, including the maintenance of essential infrastructure such as sewer systems and streets. The first \$170 billion tranche started to be distributed last year, and we are seeing that translate to new business, with our first quarter orders for sewer cleaners and street sweepers both up by more than 40% compared to last year. With the second \$175 billion tranche expected to be distributed this year, including multiyear appropriation and spending deadlines, we expect to see a prolonged meaningful tailwind from these stimulus packages. This positive sentiment was widely shared by our customers and dealer partners and recent market planning meetings.

Within our public safety end markets, demand remains strong. Our order backlog for public safety equipment at the end of the quarter was more than double that at the same time last year. We are actively working to try to reduce the current lead times in backlog.

On the industrial side, with the recent increase in oil prices, we have seen higher demand for many of our ESG products, including vacuum motors, water blasting equipment, and safe digging products. In fact, our first quarter orders for safe digging trucks were up 90% compared to the prior year. Rental interest from industrial contractors was also high, and our Jetstream business reported record revenues for its water blasting equipment rentals in the first quarter.

Within SSG, we've also seen a significant uptick in quoting activity for industrial signaling equipment and warning systems. With the increased demand causing lead times for certain products to become extended, and with the need for certain customers to secure a chassis, we again saw some dealers placing advanced orders during the quarter, which could cause some distortion in the comparability of our orders as we move through the year.

Now, turning to supply chain, where, for the majority of our vehicle-based businesses within ESG, chassis deliveries from the various suppliers that we utilize have largely remained on schedule with committed delivery date. Within our dump truck businesses, where the customer always provides the chassis, we expect the flow of chassis may be volatile for the next several quarters. However, we were encouraged with the volume of chassis deliveries that we saw in March.

Shortages of hydraulics, pumps, and certain electrical components continue to make production challenging, but our teams continue to be creative and nimble in adapting and identifying solutions to these supply chain challenges. For example, our teams have secured alternative suppliers, purchased certain buffer inventory, stocked insource or reengineer products where possible, and modified production schedules based on component availability.

As we look ahead, we are closely monitoring the recent coronavirus-related lockdowns in China. While our direct exposure to sourcing from China is insignificant, the indirect impact it may have on our supply base is currently uncertain. On the geopolitical front, we have no operations in Ukraine, Russia, or Belarus, and we do not have any direct supply chain or customer exposure.

In response to the unprecedented inflationary environment, our teams continue to take proactive measures such as locking in pricing and securing availability of steel based on forecasted needs, and implementing price increases and surcharges. To date, we have not experienced significant order cancellations on the announcement of our pricing action.

Our access to labor remains strong, and our teams have built a great culture, which has helped us to differentiate ourselves in our ability to attract and retain talented and dedicated employees at the majority of our facilities. As an example, at our largest manufacturing facility in Streator, Illinois, over many years, the team has worked extensively with the local community to build awareness around job opportunities. These efforts have included partnering with local high schools and colleges to host career fairs, open shop nights, scholarship programs, weld and fabricator programs, and even high school signing days where students can declare they are joining the Vactor team. As a result of the team's continued efforts, the team has been successful in filling 40 positions to support increased volumes since the beginning of the year.

During April, we also successfully renegotiated our union contract, which covers about half of our employees at our University Park, Illinois, facility, which is home to our domestic SSG operations. Access to a strong talent base was a key factor in our decision to purchase this facility during the first quarter.

Simply stated, our access to labor is generally good and is not currently a constraint.

We have a number of ESG-related initiatives that focus on diversity, equity and inclusion. For example, we are pleased to report that 60% of our current executive officers are gender-diverse, placing Federal Signal well above the average of our industry and peer group. We also have an ongoing focus on the environment and process improvement. For example, at our manufacturing facility in Tishomingo, Mississippi, we have recently embarked on a foam reclamation project aimed at dramatically reducing the purchase of new foam, thus reducing landfill content.

I now wanted to take a few minutes to provide an update on a couple of our growth initiatives. We remain bullish about our long-term prospects with respect to safe digging, and continue to identify new applications for this technology. For example, increased demand and spend on broadband infrastructure is generating additional interest in our broad range of product offerings that can vacuum-excavate and/or convey materials in a safe and efficient manner. Our equipment is designed to meet the production capacity and maneuverability needs to complement the multiple horizontal drilling and trenching methods used to install this infrastructure below the surface.

With the infrastructure bill's \$65 billion allocation towards broadband infrastructure, we anticipate continued demand for all of our equipment that is integral to the process of improving and expanding the infrastructure.

During the quarter, we introduced the TRUVAC truck trailer, the newest product offering in our expanding safe digging portfolio. With strong order activity in the first quarter, we've already filled the majority of production slots for the year.

Electrification also remains a key area of investment. We have launched our plug-in hybrid electric Broom Bear sweeper and begun demonstrations of our hybrid three-wheel Pelican sweeper. Demand for demonstrations of these products within our dealer network remains high. In collaboration with multiple chassis manufacturers, our teams plan to begin field testing an all-electric truck-mounted sweeper later this year. Working with a number of different partners, our research and development teams continue to explore other ways to fully integrate electrification into our suite of products. As an example, within our dump truck business, our Rugby team successfully incorporated our new Vericlass (phon) body platform into a fully electric Class 7 chassis (audio interference) in March at the 2022 Work Truck Show. We expect this to be the first of several collaborations with chassis manufacturers who are seeking to demonstrate dump truck bodies or platforms on their electric chassis.

Our aftermarket business has grown to represent approximately 30% of ESG revenues, and we see additional opportunities to grow that business by expanding into new geographies we believe to be underserved.

On the acquisition front, we are making good progress integrating our recent acquisitions, Ground Force and Deist, and we were pleased with their performance in the first quarter. Our deal pipeline remains very active, and we continue to expect M&A to be an important part of our future growth.

Turning now to our outlook for the rest of the year. We remain encouraged by conditions in our end markets, the ongoing execution against our strategic initiatives, and the order trends that we've seen over the last few quarters. Although we expect the volatile supply chain environment to continue, we are encouraged with how our teams have navigated through these challenges so far this year.

With our first quarter performance, our record backlog, and current expectations of component availability, we are raising the low end of our full year adjusted EPS outlook range by \$0.04, establishing a new range of \$1.80 to \$2.00. We are also increasing the low end of our full year net sales outlook range by \$30 million, establishing a new range of \$1.38 billion to \$1.45 billion.

With our talented workforce and capacity expansions at several facilities, our businesses are well positioned for long-term sustainable continued growth once the supply chain environment normalizes. Demand for our products is at an all-time high, with federal stimulus and infrastructure legislation offering potential for further multiyear momentum.

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

Operator

Thank you.

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

Jennifer L. Sherman

Good morning Steve.

Kenneth Newman

Hey, good morning guys. This is actually Ken Newman on for Steve.

Jennifer L. Sherman

Hi Ken!

Kenneth Newman

Morning.

So, my first question is, I'm curious if you could just comment on where price costs ended up in the quarter, and just any thoughts on how we should think about price cost spread that's implied at the midpoint of the updated guidance here.

Ian Hudson

Hey Ken, this is Ian. So, as it relates to the price costs, in terms of the absolute dollars, we feel that on a year-over-year basis, the actions that we took last year effectively covered the cost increases that we saw on a year-over-year basis. So, that was actually slightly better than what we were anticipating, and the main reason for that was because we were able to ship more than we anticipated on the dump truck side of the business with the chassis flow that we saw in March. So, in absolute dollars, it was neutral; now obviously, from a margin standpoint, there was some pressure created with the inflation that we saw. As we move forward for the rest of the year, we are expecting that to continue to improve as we flush out more of the backlog and more of that shift. So yes, we are expecting margins to improve as we realize more price going forward.

Jennifer L. Sherman

I guess I'll add there, we took a number of additional pricing actions in Q1, and we should see the benefit of that as we move through the year.

Kenneth Newman

Okay. Yes, so that leads into my follow-up question, which is, just given that it sounds like the supply chain is improving a little bit better than you expected on the chassis side, obviously you're implementing more pricing actions and you expect the margins to get better from here; I just wanted to ask about the thought process about not bumping the higher end of the guidance, and just how much conservatism is kind of embedded in the higher end there?

Jennifer L. Sherman

I guess I'll make a couple comments. As we talked about, it was a rough January, and our performance improved as we moved throughout the quarter. (Audio interference) just to remind you, there are two aspects to that.

For our non-dump truck businesses, we are seeing—the situation is very similar to what it was the last time we spoke. We're getting the chassis that the chassis OEMs committed to deliver to us.

On the dump truck side of the business, where we never own the chassis, we are beholden to others, and we did see some improvement in March. As we mentioned in our prepared remarks, we expect in the dump truck side of the business for that to remain volatile as we move throughout the year.

On the non-chassis supply chain front, I would say it's about the same as it was when we (inaudible) to you six weeks ago. You can sub in different components. But, what's changed is, our teams are pretty scrappy and getting better and better at dealing with it.

So, given the uncertainty in the market, particularly around chassis availability for our dump truck business, we felt comfortable raising the low end, and we'll update the guidance as we move throughout the year.

Kenneth Newman

Understood.

If I could just squeeze one more in, I think last quarter, you had mentioned the thought about the year kind of being a 40:60 split between the first half and the second half. It sounds to me like the quarter came in better than you expected, so is that 40:60 split still kind of in play, or just how should we think about the cadence between the first and second half at this point?

Ian Hudson

Yes, Ken, I think that's still a reasonable estimate.

Kenneth Newman

Understood. Thanks, I'll get back in the line.

Jennifer L. Sherman

Thank you.

Operator

Our next question comes from Felix Boeschen of Raymond James. Please go ahead.

Jennifer L. Sherman

Morning Felix.

Felix Boeschen

Hey, morning everybody. Hey Jennifer, hey Ian.

Jennifer, I was curious if we could talk a little bit about the sustainability of the strength you've seen in the aftermarket book, again I think up 20% year-over-year. You did mention some geographic expansion maybe in that part of the business? I was hoping you could maybe expand on both commentary. What happens if new truck production increases? Do we see sort of aftermarket ebb, or how secular, how sticky is sort of this current run rate you're seeing?

Jennifer L. Sherman

The aftermarket business has a seasonality component to it, that's really driven by rentals. So, I'll start with that comment.

So it can vary, quarter to quarter. But we have a number of strategic initiatives around our aftermarket business. You referred to one of them, the geographic expansion. We're in the process of executing on that over the next several quarters, and we're excited about the opportunity that that presents for the Company.

In addition to that, we have a number of other initiatives, particularly around used equipment and around parts. We've got a project where we are actually manufacturing certain "will fit" parts. Although we're in very early stages, it's gotten off to a strong start. So, it's also just a super team. I'm encouraged by the opportunities I see for that group as we move forward.

My final comment would really be around the resilience that we've seen over the last couple years for our aftermarket business. We think that that is a critical component for Federal Signal as we move forward.

Felix Boeschen

Helpful. Then I was just hoping to follow up on the chassis supply commentary you made earlier. It sounds like, from a dump body perspective, margin ended up being demonstrably better. I'm curious, though, if you could maybe talk about predictability of chassis flow in general, maybe as it relates to your own internal manufacturing efficiencies or inefficiencies, because of that. Has that improved at all as the OEMs are talking to you?

Ian Hudson

I think, Felix, certainly for what we internally refer to as the legacy chassis-based businesses we have, so that would be the Vactors, the Elgins, what we're seeing there is that the chassis OEMs are sticking to the committed delivery dates, which helps us run a more efficient manufacturing operation. What wasn't happening last year is that that was very sporadic, and so that made production highly inefficient. So, for the majority of our vehicle-based businesses within ESG, that is staying on schedule. So, that gives us encouragement, and we can plan accordingly.

As Jennifer mentioned, the area where we have less control is on the dump truck side, where the customer provides the chassis. So, you're absolutely correct, in March we saw a noted improvement in the flow of chassis. In February, I think, we were getting about half of what we needed to fulfill the demand. That certainly improved in March. April has been on track, but again I think we're a little cautious, in the sense that we don't control the flow of chassis there. One month doesn't necessarily give us that—create a trend, but we are certainly encouraged with what we've seen.

Jennifer L. Sherman

I think what I'd add to Ian's comments are, for our Vactor and Elgin business, chassis availability is not contributing meaningfully to production efficiencies. Where we're seeing the production efficiencies is all the other components that we talked about: hydraulics, those types of components are creating those inefficiencies in the business.

Felix Boeschen

Got it. Super helpful. I'll jump back in queue.

Jennifer L. Sherman

We're getting the chassis that the OEM promised to us.

Felix Boeschen

Thank you. Appreciate it

Operator

Our next question comes from Mike Shlisky of D.A. Davidson. Please go ahead.

Jennifer L. Sherman

Good morning.

Michael Shlisky

Yes, hello. Good morning everybody.

Can I touch first on—well first of all, it was great to see such large backlog growth in the quarter. Can you maybe tell us (inaudible) how much pricing contributed to that backlog growth, and maybe also to the topline growth in the quarter.

Ian Hudson

So as it relates to the top line, Mike, if you look at the—I think we're a little over \$50 million of revenue year over year, about 18%; of that, about 11% was organic growth and about half of that came from price. So, that's for the revenue in the quarter, and then the orders would be generally in the same kind of ballpark.

Michael Shlisky

Great. Can I just turn to University Park now. I saw you bought that in the quarter, great stuff. Are there any major projects that have to take place there now you own it, that you couldn't or didn't do before, as part of this year's capital budget plan?

Jennifer L. Sherman

We've got a number of investments that are pretty low level that we're looking at in terms of both our University Park and our Elgin facilities. Elgin, as you recall, we bought in Q4. It (audio interference) focused on improving efficiencies.

Ian Hudson

But Mike, in terms of dollars, nothing of a particular magnitude. I still think we continue to expect our CapEx, absent the UP facility purchase, to be in the range of about \$25 million to \$30 million, which is more in line with what we would typically expect. So, nothing significant in terms of CapEx required at UP.

Michael Shlisky

Okay. No disruptions or shutdowns planned for that facility either, correct?

Jennifer L. Sherman

No.

Michael Shlisky

Okay, perfect.

Then just turning back to the backlog quickly, I wanted to touch on the timing as well. I know you've had great growth; is all that backlog planned for 2022 delivery? Is the tenure of the backlog longer or shorter than you normally would have?

Ian Hudson

So, not all of it will ship in '22, Mike. Again, it varies by product line, but we are—for sewer cleaners in particular, where we've seen some really strong demand, we are looking at into the first quarter of '23. The lead times are longer than we would like them to be, and we are actively trying to work those down with the challenges and the constraints on the supply chain. But, they're a little longer than we would like them to be, so we are trying to work those down.

Michael Shlisky

I guess to clarify there, are you hearing from customers that they want to make a multiyear order or commitment to get a better place in your production schedule? Are they looking to plan ahead further than they have in the past? I'm just kind of curious if people are prioritizing this type of equipment more than they have in the previous years.

Jennifer L. Sherman

We have very few multi-year orders. As we noted in our prepared comments, we do have certain customers that we believe have placed their orders earlier than they might otherwise, because of our extended lead time. However, we take a close look at demand, and it's really been across the board, and we believe that, between the infrastructure bill and the American Rescue Plan, that that will provide kind of multiyear tailwinds for our equipment.

Michael Shlisky

Got it. Got it. Well, thanks so much, I'll pass it along. I appreciate it.

Jennifer L. Sherman

Thank you.

Operator

Our next question comes from Chris Moore of CJS Securities. Please go ahead.

Jennifer L. Sherman

Good morning Chris.

Daniel Moore

Hi, good morning. It's actually Dan Moore for Chris. Good morning Jennifer, good morning Ian, thanks for all the color.

Maybe start with: is there any way to roughly estimate how much margin was lost in Q1, relative to the inefficiencies caused by the supply chain issues as well as COVID within your plants?

Ian Hudson

Dan, it was primarily felt within ESG, and you'll see, obviously, the impact on the gross margin that we had within ESG, we were down about 170 basis points. Most of that was driven just from the inefficiencies we had primarily in January, a little bit into February. The other factor would be, obviously, the price cost impacts. While in absolute dollars we were effectively neutral on a year-over-year basis, there was some margin pressure created from that dynamic.

The other thing that impacts the margin within ESG is we had a higher concentration of chassis that we supply, and that's with our efforts to go out and procure more chassis. We actually had more chassis revenue, which has a dilutive margin impact. So, there was about \$6 million of additional chassis revenue on a year-over-year basis, which had an impact on the gross margin within ESG.

So, those are the kind of three main drivers within the margin change that you see in Q1 within ESG.

Daniel Moore

Very helpful; and then, you mentioned that the 60:40 split between H2–H1 still holds. Any additional color or commentary on just the cadence over the next—over that timeframe, given the various moving parts, including some of the price increases that you're still putting through, how should we sort of think about that margin walk implied in the guidance? Thanks.

Ian Hudson

I think, Dan, if you look back at the historical patterns driven by some of the seasonality of our aftermarket business, Q2 and Q3 tend to be strong, with Q3 probably being the strongest, in terms of the aftermarket business just with a lot of the work taking place in the summer months, strong rental activity. So, we continue to expect that. Then Q4 is typically strong as well on the municipal side; SSG typically has a strong finish to the end of the year, so. I think those dynamics, in terms of the walk for the rest of the year, we would expect similar patterns on the aftermarket business that we've seen in prior years.

Daniel Moore

Got it. Then lastly, it doesn't sound like it, it sounds like demand remains strong across the board and rising. But any impact that you can discern from a rising interest rate environment on demand at this point, or any of those discussions with customers, or is it more about getting as much product as they can? Thank you again for the color.

Jennifer L. Sherman

Yes. We haven't seen impact in terms of demand for our customers. I think one of the factors that differentiates us from others is just the wide range of our portfolio offerings. So, obviously we have new equipment, we've got used equipment, rentals, which we talked about were really strong. So, strategically, a critical initiative has been that we've got the solution for our customers that we can tailor to their specific needs. We believe that will continue to prove to be beneficial as we move forward.

Daniel Moore

All right. Thanks again. Best of luck for the remainder of the year.

Jennifer L. Sherman

Thank you.

Operator

Our next question comes from Greg Burns of Sidoti & Co. Please go ahead.

Jennifer L. Sherman

Good morning, Greg.

Gregory Burns

Good morning. Sort of a follow-up a little bit on the chassis. So, it seems like your suppliers are able to produce to what they promised, but are you seeing anything in terms of maybe potential for improvement, or them to be able to actually increase the supply of chassis to you, or anything in the conversations you're seeing, or anything out in the macro or in the industry, that would give you hope that maybe you start to see some increase in availability?

Jennifer L. Sherman

Again, I want to divide my comments into two sections, so first I'll talk about Vactor, Elgin, our legacy businesses, which is a different experience than the dump truck businesses. So, on the Vactor/Elgin side, as we talked about, we're getting what the chassis manufacturers promise, but we are in allocation. We have been successful in terms of going out and procuring some additional chassis outside the normal channels, so right now chassis are not our constraint for those businesses, it's really the other component parts, primarily hydraulics. So, if we were to see some relief with respect to those other component parts, and hydraulics is just one example, we're very focused on reducing our lead times and reducing our backlogs, because they're longer than we'd like them to be.

On the dump truck side of the business, where we don't supply the chassis, we, again, are beholden to our customers and dealers to supply those chassis. As Ian mentioned, we saw improvement in March; one month does not make a year, and we continue to monitor that situation. But again, we are very focused on reducing those backlogs.

Gregory Burns

Okay; and then, in terms of the oil and gas market, can you just maybe quantify the size of that business and relate that maybe to the last time we saw oil spike, how big that business got for you at that time; and

then lastly, how your business might be better positioned this time around, maybe with some of the new products you have or the stronger aftermarket to capitalize on that opportunity?

Ian Hudson

So, in terms of the current contribution, Greg, it's probably—we'd estimate it's in the range of \$20 million to \$30 million of revenue. If you go back to the peak between 2015 and 2016, when oil fell pretty significantly, we estimate we lost about \$80 million of revenue. That was primarily when all we did was sell new equipment, and that was largely in the safe digging vehicles.

So, since that time, we've seen some of that revenue change in terms of shifting more towards rental income and used equipment sales. So, we think—we certainly have seen renewed demand from oil and gas customers on the rental side, there's heavy interest in our safe digging trucks in the rental fleet, which is a large component of our own rental fleet. We've also seen that with our rental partners as they look to replenish fleets, with strong used equipment sales out of those fleets.

So, it's certainly not back to the levels it was at the peak, but in terms of the direction it's heading, there's some momentum there, albeit I don't think we'd expect it to get back to the same levels that we saw in '15 and '16, and because the nature of the revenue has changed, shifting from new equipment sales to more of the rental and used equipment sales as well.

Jennifer L. Sherman

Other products that increasing oil prices can have a positive impact on would include our Jetstream product, our Guzzler products, and a small portion of our SSG products.

Gregory Burns

Perfect, thank you.

Operator

Our next question comes from Walt Liptak of Seaport. Please go ahead.

Jennifer L. Sherman

Good morning.

Walter Liptak

Hi, good morning, thanks.

So, great quarter. Maybe a follow-on to the last one about the O&G related product. I think you threw out a number that Truvac orders were up 90%? Wonder if you could help us with that: does that mean it went from like 15 or 20 up to 30, 40? What's the level that we're at?

Ian Hudson

Well, it's more in the \$35 million to \$40 million range in terms of the orders in the quarter. Again, when we gave those stats, that is just talking about the pure play Truvac trucks; that does not necessarily include the sewer cleaner trucks that I think—many of those, or the majority of those now, of our sewer cleaner orders come with a hydro package, so you can almost use it as a multipurpose vehicle. So if you look at

that as well, those sewer cleaner orders in the quarter, they were up 43% which is about \$20 million of year-over-year improvement. So, the combination of those two are really an indication of the growth that we're seeing on the safe digging side of things.

Jennifer L. Sherman

We also saw Truvac demonstration increase Q1 of this year versus last year, which is an encouraging sign also. Then we introduced—we continue to expand our portfolio of Truvac products with the introduction of our trailer trucks product.

Walter Liptak

Okay, yes, that's great, that's good to see. What's the price differential between the Truvac truck and one of the trailers? Maybe as a percentage, you don't have to give me a round number, but ...

Ian Hudson

Oh, the trailers life (phon), it's fairly small in terms of the contribution to that 90%. It's relatively small because it's a brand-new product we've just introduced. So, in terms of the dollar amount of that, it's fairly small right now. But we're looking to grow it as we generate more interest in the product.

Jennifer L. Sherman

We introduced it at the WWETT show in February, and we're currently demoing the product, and we're taking orders for the product for this year. But we're in very, very early stages on that initiative.

Walter Liptak

Okay. Okay great. I guess my question was, is that half the price of the Truvac or three quarters of the price of the Truvac for the trailer?

Ian Hudson

It's significant—well, in terms of the price, it's significantly less than a truck-based product. We're talking more in the 80 to 120 range for the trailer, whereas the full-size trucks can certainly be multiples of that.

Walter Liptak

Okay. Got it.

Jennifer L. Sherman

It just gives us another—it's a new end market for us. It gives us another opportunity for stickiness with our customers.

Walter Liptak

Okay, great.

Then, on the point that you made about rental, the shift towards rental for the O&G markets this time around, could you provide a little bit more detail about why you think that is? Are you picking up more

rental customers, or is it your rental that you're pushing? Like why is it that this time around the service providers will be renting more trucks than owning them?

Jennifer L. Sherman

Well, if you go back to 2016, there just weren't—there are many more trucks available now. The rental business for our products was really in the infancy. So, there are a lot more trucks available, both from us and our valued rental partners. So, that's an important component as we look at those numbers.

We also see, this is an alternative. Again, some end customers rent, some end customers rent to own, but it gives them an opportunity to either supplement their equipment or, depending on the nature of the project, it gives them an opportunity to rent to own in some situations.

Walter Liptak

Okay. All right, great.

In your commentary about M&A and your—it sounds like you've got capital available, and you're continuing to build the funnel for M&A. Does the supply chain issues and all the inflation that we've gone with, does that cause you to pause at all on M&A, or are you still just as active as you were before last year when everything tightened up?

Jennifer L. Sherman

I think we've proven to be very disciplined acquirers, and we're going to continue to employ that same methodology. But our M&A pipeline is active, and we believe that it will be a meaningful part of our growth story going forward.

Walter Liptak

Okay, great. Okay. Thank you.

Jennifer L. Sherman

Thank you.

Operator

Our next question is a follow-up from Steve Barger of KeyBanc Capital Markets. Please go ahead.

Kenneth Newman

Hey thanks. This is Ken Newman. Appreciate the follow-up here.

I just wanted to follow on to the rental comments just now. I guess I'm trying to get a better sense of what the expectation for rental growth is into the second quarter and to the second half. Specifically, just any color you can give in terms of how much of that is coming from better fleet growth versus higher rental rates? I imagine the time utilization for those fleets is pretty tapped out at this point. But any color there would be helpful.

Jennifer L. Sherman

There's a couple components driving it. One, as we talked about, there's the seasonality component. Typically Q2 and Q3 in the warmer months in the northern part of North America will see higher time utilization and financial utilization. The Canadian market is an important part of our rental fleet and rental fleet opportunities. The second would be the—we have seen increase in rental rates by both us and our rental partners, and then we have made some additions to the rental fleet, and that can fluctuate from quarter to quarter depending on how much we sell out of the fleet and the needs of the customers. We also talked about, as a critical strategic initiative for the aftermarket group, geographic expansion, so that also creates additional opportunities for us.

Kenneth Newman

Is there any way you can quantify just how much of the backlog is slated for the rental fleet versus true third-party deliveries?

Ian Hudson

Yes, Ken, the backlog that we cite is all external. We don't include, in what we talk about externally, anything that's going into our own rental fleet.

Kenneth Newman

Understood.

Then my last follow-up here is just kind of also an idea of just how we should think about your expectations for aftermarket growth at this point. Obviously it's been very strong, given the tight supply chain dynamics. Is there further upside, or just how much more do you think you can be flexing on price, just given how tight the supply chain is, and whether you're seeing any pushback from pricing pushes on the aftermarket side at this point.

Ian Hudson

I think, Ken, aftermarket has grown now, Ken, to be about 30% of ESG's revenues. There's potential upside to that, I think certainly as you look at the demand and the interest we've seen in the rental fleets in Q1, which is typically the softest quarter in terms of rentals, that's been encouraging.

The other thing I would say is on the parts side, where maybe with the lead times extended, new equipment lead times are pretty extended. So, people are refurbishing their existing equipment, and that's then translated into increased part sales. So parts, which is the largest component of what we call our aftermarket revenues, that was up about 14% in Q1 versus Q1 of last year.

So, I think we'll continue to see a lot of interest in parts, as well as rentals and used equipment sales, just with the current environment where chassis lead times are extended and so are the lead times for some of our own products. So, we may see that tick up a little bit over 30%, and that's really why we believe that this is a very important strategic initiative for us.

Jennifer L. Sherman

Also I believe that the infrastructure bill will create additional opportunities, not only for whole goods sales as we've talked about, but also for our aftermarket group.

Kenneth Newman

Yes, that makes sense. I appreciate the time.

Jennifer L. Sherman

Thank you.

Ian Hudson

Thanks Ken.

Operator

Our next question is a follow-up from Walt Liptak of Seaport. Please go ahead.

Walter Liptak

Hi. Thanks for taking my follow-up too.

Jennifer L. Sherman

Of course.

Walter Liptak

I wonder if you could help us with understanding the 2022 guidance and the low end. So, my question is, if you were to come in at the low end of the range, why do you think that would be? Is it because you have like an increase in supply chain problems again, or another round of Omicron, what do you think it is that would get us to the low end?

Jennifer L. Sherman

The chassis situation at TBEI that we talked about, we expect it to be volatile, although we were encouraged by March. So, there's uncertainty there. You referenced Corona virus, if we saw something like we saw in January and lost 20,000 production hours, that could be another issue. The final issue that we're monitoring that we talked about is, given the China shutdown, although we don't have a lot of direct exposure, the chassis OEMs, if there was another microchip issue and we stopped getting the chassis that have been promised to us for our Vactor, Elgin and other vehicle-based businesses, that could also be a problem. So, all of those are baked into the low end of that guidance.

Walter Liptak

Okay. All right, great. Thank you.

Operator

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

Jennifer L. Sherman

In closing, I would like to reiterate that we are confident in the long-term prospects for our businesses and our markets. Our foundation is strong, and we are focused on delivering profitable long-term growth to the execution of our strategic initiatives.

We would like to express our sincere thanks to our stockholders, employees, distributors, dealers, and customers for their continued support. Thank you for joining us today, and we'll talk to you next quarter.

Operator

This concludes today's conference call. You may disconnect your lines. Thank you for participating, and have a pleasant day.