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RPM - Q2 2019 RPM International Inc Earnings Call

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OVERVIEW:

RPM reported 2Q19 sales of $1.36b.

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PRESENTATION

Operator

Good morning, and welcome to RPM International's conference call for the fiscal 2019 second quarter. Today's call is being recorded. This call is also being webcast and can be accessed live or replayed on the RPM website at www.rpminc.com.

Comments made on this call may include forward-looking statements based on current expectations that involve risks and uncertainties which could cause actual results to be materially different. For more information on these risks and uncertainties, please review RPM's reports filed with the SEC.

During this conference call, references may be made to non-GAAP financial measures. To assist you in understanding these non-GAAP terms, RPM has posted reconciliations to the most directly comparable got financial measures on the RPM website.

(Operator Instructions) Please note that only financial analysts will be permitted to ask questions.

At this time, I would like to turn the call over to RPM's Chairman and CEO, Mr. Frank Sullivan, for opening remarks. Please go ahead, sir.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Thank you, Brandon. Good morning. Welcome to the RPM International Inc. investor call for our fiscal 2019 second quarter ended November 30, 2018. On the call with me today are Rusty Gordon, RPM's vice president and chief financial officer; and Kristine Schulze, our senior director of financial reporting.

I'll kick the call off by providing some broad perspective on our second-quarter results, and Kristine will run through our numbers in more detail. And she'll be followed by Rusty, who'll provide a progress report on operating improvement plan and an outlook to the balance of the year. After which, we'll be happy to answer your questions.

For the second quarter, we generated solid top-line sales of $1,360,000,000, reflecting an organic increase of 3% and acquisition growth of 2.6% over last year's second quarter. Current-quarter sales also include the unfavorable foreign exchange impact of 2%. Growth was fairly well balanced between organic initiatives and acquisitions, while foreign currency translation obviously reduced sales. Organic sales growth was evenly spread across our 3 operating segments, which demonstrates the value in our approach to deliberately maintaining a strategic balance between our segments and a focus on growth as we pursue our 2020 MAP to Growth initiative.

Near-record wet fall weather resulted in disappointing sales at Tremco Roofing, Dryvit and various consumer segment products with exterior use. We believe this weather-related impact is temporary. From a geographic standpoint, we experienced disappointing international results across most all of our business, particularly in Europe, which was also aggravated by the unfavorable foreign exchange.

Our gross profit margin was impacted by raw material costs in the quarter once again. As mentioned last quarter, our businesses have been executing price increases to combat the pressure put on margins by raw material cost increases, which have been rising now for six consecutive quarters. We anticipate that raw material costs will level off in the back half of our fiscal year and that our businesses will further close the gap on our margins, with price increases that have been negotiated and will be instituted in the coming months.

We continued to rein in expenses during the quarter. Better cost control led to an adjusted SG&A-to-sales ratio improvement of 100 basis points over the second quarter last year, on an adjusted basis.

Regarding our MAP to Growth operating improvement plan, we continue to make good progress. This quarter, we announced five additional manufacturing plant closures and eliminated another 149 positions. We began the transition to center-led manufacturing and procurement and we're moving forward on our supply chain initiatives, where we're starting to consolidate the number of vendors and negotiating more favorable terms and pricing.

During the first half of our 2019 fiscal year, cash from operations improved by 29%, a direct result of improved working capital management. While our bottom line results were disappointing, we're pleased with our solid top-line growth, the anticipated margin improvement to come from our improving raw material cost-to-price ratio and the benefits we expect to experience as we continue to implement our MAP to Growth initiative.

I'd now like to turn the call over to Kristine Schulze, RPM's senior director of financial reporting

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Kristine Schulze - *RPM International Inc. - Director of Financial Reporting*

Thanks, Frank, and good morning, everyone. During our fiscal 2019 second quarter, we reported restructuring and other onetime charges totaling $29.2 million. As further detailed in our earnings release, the largest component of these adjustments, or nearly $23 million, relates to our MAP to Growth initiative. Of these MAP to Growth charges, nearly $7 million is related to severance; $6 million resulted from restructuring-related professional fees and ERP consolidation expenses; and the remaining amount is associated with our manufacturing consolidation initiative.

I will now review results of operations for our fiscal 2019 second quarter on an as-adjusted basis. During the second quarter, our sales were a record $1.36 billion, up $47.1 million, which was a solid 3.6% increase over last year's second quarter. Organic sales grew 3% and acquisitions added 2.6%, which was offset by foreign currency translation of 2%. Our earnings were impacted by several factors, which included: continued raw material cost challenges, investment losses resulting from a new accounting standard and the unfavorable foreign exchange impact of the strengthening U.S. dollar.

As we anticipated on last quarter's call, raw material headwinds persisted in the second quarter. In particular, we continued to experience significant challenges with the cost of silicones, asphalt, epoxy and acrylic resins, while cans and other packaging continued to rise modestly. However, we continued to successfully institute price increases and were able to narrow the gap on our margins. We also noted that an unfavorable product mix and higher inbound freight contributed to the slide in our margin.

Sales in our industrial segment increased 2.1% to $718 million, reflecting organic growth of 3.3%, and acquisitions contributed an additional 1.5%. Foreign currency translation reduced sales by 2.7%. The segment benefited from solid performance in our businesses providing corrosion control coatings, North American construction sealants and concrete admixture and repair products. This was achieved despite the impact of the second wettest autumn on record in the U.S., which affected sales, particularly in our commercial roofing business. International sales, which account for approximately half of our industrial segment business, were soft this quarter.

On the bottom line, higher raw material costs and unfavorable foreign exchange impacted results. We made good progress on our operating improvement initiatives in the segment, which included progress towards consolidating production with the announced closure of three plants. Adjusted EBIT in the segment increased 1% to $70.9 million from last year's second quarter.

In our consumer segment, sales increased by 4.1%, which was fairly evenly split between organic sales growth of 2.8% and acquisition growth of 2.9%. Foreign currency translation reduced sales by 1.6%. Organic sales growth was aided by new account penetration, which offset poor POS performance resulting from exceptionally wet weather in the United States, the segment's largest market. Adjusted EBIT was $42.9 million.

Price increases instituted late in the first quarter helped to slow margin erosion in the consumer segment. However, raw material cost continued to be a challenge. Operational improvements, which began during the fourth quarter of last year, continued to be made in the segment and are leading to working capital improvements. Also, we announced the closure of one additional manufacturing facility during the second quarter.

Specialty segment sales grew at a strong 7.6% pace. This was driven by acquisition growth of 6.1%, primarily from the September acquisition of Nudura, a manufacturer of insulated concrete forms that expands our Dryvit product line offerings. Organic growth contributed 2.3% to sales, while foreign currency translations had a modestly unfavorable impact of 0.8%. Driving organic growth were our businesses providing wood coatings, powdered coatings and florescent colorants.

Specialty results were better than expected, since the prior-year comparison was a tough one. Performance by our restoration equipment business was brisk as it responded to recent national disasters, but was below elevated sales levels that resulted from Hurricane Harvey last year. We made MAP to Growth progress in this segment as well with the announced closure of one manufacturing facility. Adjusted EBIT was $34.1 million during this year's second quarter.

During the quarter, our stock performance enabled us to redeem our 2.25% convertible senior notes due 2020, which was completed on November 27, 2018. By utilizing mostly cash for the redemption. Going forward, this will have the impact of reducing our diluted share count by 3.3 million shares while being debt-neutral to RPM. On a related note, we repurchased approximately $82 million of our common stock through November 30, 2018, which is in line with our plan to return $1.5 billion in capital to our stockholders by May 31, 2021, through a combination of dividends and share repurchases.

I'll now turn the call over to Rusty for some details on our outlook for the remainder of fiscal 2019.

Russell L. Gordon - *RPM International Inc. - VP & CFO*

Thanks, Kristine. We remain focused on executing our MAP to Growth operating improvement plan, targeting a 540-basis point improvement in our operating margin. As we announced on November 28, 2018, we intend to return $1.5 billion in capital to our stockholders by May 31, 2021, through a combination of dividends and share repurchases. In addition to the previously mentioned convertible bond redemption, we have repurchased approximately $82 million of our common stock through November 30, 2018.

Additional actions we completed during our fiscal 2019 second quarter include the announced closure of five manufacturing plants, the reduction of 149 positions and the start of our transition to center-led manufacturing and procurement functions. We also began to implement tactics to improve our manufacturing processes, optimize assets and reduce inventory, while moving forward on our supply chain initiatives to consolidate the number of vendors used and negotiate more favorable pricing and payment terms. Accordingly, we are maintaining the long-term projections that we provided at our November 28 Investor Day.

In regards to our sales outlook for fiscal 2019, we expect full-year fiscal 2019 industrial segment sales to grow in the mid-single-digit range as it benefits from steady commercial construction activity and a recovery in the oil and gas market. In our consumer segment, we anticipate sales growth in the mid- to upper-single-digit range resulting from recent market share gains and stepped-up advertising to support new product placements. In our specialty segment, we expect sales growth in the low-single-digit range. We have additional price increases negotiated recently, which are scheduled to be implemented in February and March as we look forward this year.

I will now comment on our expectations for the third quarter of fiscal 2019. From an operating perspective, revenue growth should remain in the low- to mid-single-digit range, with FX headwinds remaining a challenge. While we are seeing the early benefits of our purchasing activities and softness in certain raw material categories, it is important to note that RPM is on a FIFO basis for inventory, which means that the benefits we are beginning to see on the raw material front will typically flow into our income statement 90 days later than if we were under the LIFO method of accounting, as is the case with our larger industry competitors.

Due to three nonoperating items, we anticipate significantly lower reported earnings and earnings per share for the third-quarter period ended February 28, 2019. These items are the following: number one, an anticipated current tax rate of approximately 26% versus a benefit from certain tax items of $5.9 million last year; number two, while gains were realized in the prior year on sales of marketable securities, we expect a different result this year due to the combination of declines in the equities market in December and the new accounting standard, which requires unrealized gains and losses on equity securities to now be reflected in earnings, we anticipate a year-over-year negative impact during this year's third quarter to be in the range of $5 million to $6 million; and number three, an adverse comparison to last year's third quarter when we reversed approximately $3.4 million of long-term incentive compensation when it became clear that the targeted goals would not be reached.

Taken together, expectations of continuing raw material cost challenges and these nonoperating items are likely to result in third-quarter EPS in the range of $0.10 or $0.12 per share.

Although we are in the early innings of our restructuring efforts, we are making good progress, which has us excited about the prospects for the future. As we work through the plan over the next few quarters, we will continue to adjust out associated charges to provide a clear picture of the initiative and the progress we are making.

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

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Thank you, Rusty. I'd like to do a brief review of our 2020 MAP to Growth initiative, starting with our 2020 MAP to Growth timeline. The program was kicked off in the spring of 2018. In June of 2018, we reached a settlement agreement with Elliott Management. We added two new directors, we've formed an operating improvement committee, which met three times over the summer to assess the opportunity and program design. A full report was made to the RPM board in early October, and we communicated our 2020 MAP to Growth initiative to our global leadership team in early November, and obviously had an investor communication on November 28.

What have we accomplished? From a manufacturing perspective, including two plant closures in the second quarter of last year, five announced plant closures in the first quarter, an additional five announced plant closures in the second quarter of fiscal '19, we have announced and are in the process of completing the closure on 12 manufacturing plants. This is also driving the closure of nine warehouses and nine related offices.

From a procurement perspective, as of today, we have had meetings with vendors who represent approximately $400 million of what we believe is $1.5 billion of an addressable spend to discuss pricing and terms. By the end of February, we expect to have met with or addressed, from an in-sourcing or strategic perspective, approximately $1 billion of our addressable spend.

I'd like to make a comment on the second-quarter raw material costs with some specifics. Our top 10 raw materials, second quarter of this fiscal year to the second quarter of the prior year, were up 10% -- I'm sorry, 18%. A couple of these specifics include silicones, which year-over-year, are up 61%; and epoxy resins, which were up 31%. The second quarter sequentially versus the first quarter, we see our top 10 materials down 1%. Without addressing any additional specifics, the point is we have more timely and better data across purchasing categories and manufacturing costs in more hands than we've ever had, and that's also a direct result of the improvements of our operating initiatives.

With those comments, we would now be happy to take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And from Bank of America, we have Steve Byrne.

Steve Byrne - *BofA Merrill Lynch, Research Division - Director of Equity Research*

I just wanted to see whether or not your projected cost savings from your MAP to Growth program are going to be adequate to hit that 16% EBIT margin target, given it seems like you're in a little bit of a deeper hole in your margin right now. Is that -- is it still on track to hit that 16% margin by the end of fiscal 2021?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. As Rusty commented, I think we feel pretty good about our longer-term targets in the MAP to Growth program. And also, as he mentioned, we expect, starting with our April call, we'd actually be able to provide some more detail. We want to be able to do a rearview mirror lookback that provides detail, for instance, on manufacturing and sites, once those have actually been completed. It's the right way to do it to keep our people focused on execution and also the right way to handle communication flow. We'll be in a position to do the same thing in other categories. And so far, we're on track in every category that we're focusing on.

Steve Byrne - *BofA Merrill Lynch, Research Division - Director of Equity Research*

And just one high-level question for you, Frank, on this MAP to Growth initiative. Your investor event down in Baltimore was certainly useful at drilling into all of your businesses. But one comment I have is that every one of them seems to be headquartered in a different city. And I just wanted to hear your views on the potential merits of an integration that includes the commercial infrastructure and the -- all of the back-office headquarters of all these businesses. Is that on the table as well?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

So as it relates to our structure from a sales and marketing perspective, as we commented, we're big believers in the entrepreneurial approach that's been successful for RPM. I think the organic growth that we're generating in this quarter and this year is reflective of that. And we do not see any benefit long-term of consolidating sales force or marketing or product development activities. On the flip side, we are keenly focused on consolidating much of the G&A and accounting and ERP systems into the four groups that we've outlined on November 28, and we're making good progress on that. We'll have more details on that, again, in April. I can tell you that we have been working with our internal team in terms of some new hires and some promotions and with AlixPartners on the manufacturing and operating perspective. And we are very much on target. We're very happy with the progress there. On the G&A side, we didn't seem to have the same enthusiasm in terms of the outside resources, so we have talked to a number of other firms and we have engaged an additional firm to help us with the combination of consolidation in the G&A area and also opportunities for outsourcing. So, we are continuing to advance the ball, both on the original program, and in ways that we can accelerate or enhance it.

Operator

From BMO Capital Markets, we have John McNulty.

John McNulty - *BMO Capital Markets Equity Research - Analyst*

At the Investor Day, you spoke on procurement and raw material saves, and I think one of the baskets was just the commodity cycle recovering and essentially catching up to the raw materials, whether the raws fell or the pricing went through. And if I remember, the basket was somewhere in the $65 million to $80 million range. I guess it looked like that was scheduled for kind of a wave 2, wave 3, which was 2021, 2022, but we've seen commodity prices fall pretty dramatically here. So I guess the question is, if you kind of look at what your commodities are looking like right now in terms of raw materials, how much of that do you think you may see a couple years earlier than originally expected?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

So the MAP to Growth initiative highlighted approximately $75 million to $80 million of savings that we believe we can get from a different approach to procurement over wave 1 and wave 2, which is really between now and the end of May 31, 2020. And there was a $65 million number, which we highlighted as commodity cycle recovery, and we're pretty agnostic as to how much it would be ultimately and when it would hit. I guess what I would say to that is just to refer back to the comments I made a minute ago. Year-over-year, we're still getting hit pretty significantly. Second quarter, top 10 materials were up 18%, I highlighted a couple of the extreme examples. Sequentially, the top 10 materials are down 1%. That's not going to -- as Rusty highlighted in his outlook, we're still going to be facing a year-over-year significant raw material increase relative to the third quarter last year and the third quarter we expect this year. We are seeing some softening in certain categories. There are still some other categories that are going up. And the underlying dynamics, whether it's oil prices or propylene or other things, are certainly moving in the right direction, that suggest the commodity cycle improvements certainly should be coming before what we had as wave 3. So, we ought to benefit from those, with the entire industry. We're also working internally on data to be able to track the difference between the structural procurement benefit changes and what would be coming in relationship to commodity cycle improvements, anyways.

John McNulty - *BMO Capital Markets Equity Research - Analyst*

Got it. And then on the industrial side, I know there is -- it's a seasonally light quarter for you in terms of what you're in right now, but I guess, can you give us an update as to what you may be seeing there? And I know you had indicated, I guess, on the guidance for the full year and sales, that one of the areas where there was some hope was on the energy markets. And I guess with that market coming under some pressure, I guess, I'm wondering what kind of demand trends you're seeing there, if there's been any change at all.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Yes. I think the biggest disappointment in our industrial business was weather-related. Our Tremco Roofing business, which has been very strong; Dryvit, which is, again, all exterior cladding, both had weak second-quarter results, a lot of that was weather-related in terms of a very wet fall. I think weather also negatively impacted, as I said, the kind of exterior-related products of our consumer segment. We think that's temporary. The more challenging area for us in terms of revenue disappointment was international, in particular, Europe, which seems to be slowing down. And I'm not too sure that, that is temporary. But when you put all that together, we had real solid organic growth in a lot of our construction categories, in corrosion control coatings and floor coatings, which obviously exceeded the industrial segment average, based on the challenges that we saw, weather in some categories and some international weakness. We feel pretty good about that, and we feel pretty good about the progress we're making between raw material cost increases and price as the subsequent quarters are executed.

John McNulty - *BMO Capital Markets Equity Research - Analyst*

Great. And then just one last question, just on the Home Depot rollout, I guess, can you give us an update as to how that's progressing? Again, I know it's a seasonally relatively weak period, but be curious how that's moving along.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. Consumer takeaway across most of the categories we're in has been relatively flat all year. I think there's a lot of belief that some of that's been weather related. We continue to pick up some market share in the interior wood stains and finishes category. We are exceeding our expectations, we're exceeding our customers' expectations. And in a couple regions, we're well ahead of the brand that we replaced. So that program is off to a great start. As it relates to pricing across all of our categories, as folks on the call know, we had some major line reviews and some new category pickups, all of which came with some price commitments that precluded us from pursuing appropriate price increases in certain categories until those line review wins or new category pickups were annualized. That will happen this spring, and those negotiations are underway.

Operator

From Great Lakes Review, we have Jason Rodgers.

Jason Rodgers - *Great Lakes Review - VP*

Would you be able to quantify the price increase benefit you experienced in the quarter and the expectation going forward?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

About 2% on the quarter. And I think you'll see the same and a little bit growing in the coming quarters.

Jason Rodgers - *Great Lakes Review - VP*

And I was interested in your progress with the ERP consolidation. And perhaps, you can discuss the timeline for implementation there.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Yes. I don't think we'll have that completed until the end of our MAP to Growth program. So, you're looking December of 2020 or even into the spring of 2021, so by the end of our '21 fiscal year. We're making solid, steady progress. We chose the path we did because we did have four core systems that -- where we are consolidating to. People are very comfortable with those. So, in our construction products categories, SAP; in consumer, SAP; and then Microsoft D 365 in specialty; and Baan LN in our performance coatings group. And so, it's really slow progress. I think the tailors will be smaller international operations by the end of December 2020 with what will represent somewhere in the neighborhood of 80% to 90% of our revenues.

Jason Rodgers - *Great Lakes Review - VP*

All right, that's very helpful. And it might be too early to ask this, but wondered if you were getting any early feedback on the daily performance standards you're implementing at the plants.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Absolutely. We are -- aside from the plant closures that I talked about, we are instituting the operating improvement and continuous improvement program across our plants. In the second quarter, we had three, what we call, fit events, which are focused manufacturing events. And we are instituting metrics that are consistent across our businesses. And we are measuring, month-by-month, the performance to those metrics. And we will be in the next 12 of our largest plants in the current quarter. And we are marching through our plants and we are measuring and we are seeing progress that makes us comfortable that we will meet or exceed the operating improvement targets that we laid out in November 28, both as it relates to consolidation and as it relates to platform improvement. And the last thing I'd mention is that we -- one of the real benefits of what we're doing is we have access to data on the procurement side and the plant side in more leadership hands. It's more timely and more accurate than we've ever had, and that's incredibly helpful.

Jason Rodgers - *Great Lakes Review - VP*

All right. If I could just squeeze in a numbers question. If you have an estimate for CapEx for fiscal '19 as well as a targeted amount of share repurchases for fiscal '19.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

So I think for fiscal '19, we'll be flat to slightly up over last year. And in terms of share repurchases, I'd be hesitant to put out a target, but we certainly were a re-purchaser of our stock in the mid- to low $60s, and I would expect us to be a re-purchaser of our stock where it is today. And we are very much committed to the return of capital targets that we put forth in November 28.

Operator

From Gabelli & Company, we have Rosemarie Morbelli.

Rosemarie Pitras-Morbelli - *G. Research, LLC - Research Analyst*

Frank, I was wondering if, as you are going through your MAP project, if you are seeing some kind of disruption on your operations, which would result or have resulted in slower growth than you anticipated outside of the weather impact. I'm assuming that it has to be disruptive.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Yes. I'm not aware that we're seeing disruption on the sales front. I think there's a couple of areas where we're doing some reorganization, for instance, in Europe, where we've got some work to do and some opportunities that were perhaps bigger than we realized. And so, we've had some leadership changes in certain areas, and that can certainly be disruptive. And we're moving to get the right leaders in the right places so that we can be properly focused. But in general, I think the enthusiasm for this program is across RPM, and we're continuing to see pretty solid revenue growth.

Rosemarie Pitras-Morbelli - *G. Research, LLC - Research Analyst*

Looking at Europe slowing down, can you give us a better feel for which areas are feeling most of the impact, and what you are doing to offset it. Any new steps versus those you have expressed on November 28?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

I think the slowdown in Europe is pretty universal. We're seeing it across most all of our business categories. So, unlike what we feel is some weather-related impact on revenues in the second quarter in the U.S. is temporary, I would expect us to see relatively flat growth in Europe for the balance of the year. And beyond that, again, I think we'll be in a position as we get things executed and realize, to talk in hindsight in more detail. But we have a pretty intense focus in a number of areas, including Europe, in terms of some G&A consolidation and also the manufacturing and operations work that is happening across RPM.

Rosemarie Pitras-Morbelli - *G. Research, LLC - Research Analyst*

And if I may ask one last one. As raw material costs are coming down, do you think that you can still achieve your price increases?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Raw material prices are coming down, as I said, 1% in the second quarter versus the first quarter. They're up 18% year-over-year. And in certain categories like silicone, which is a critical component, for instance, for our DAP business, consumer DIY, and in our Tremco business, those raw materials are up 61%. They are not softening. There continues to be some capacity issues there. So, the raw material situation today is a real mixed bag. There are some improvement in some packaging areas, but in other packaging areas particularly related to steel and/or rigid packaging, you're continuing to see some price issues. So, it's a mixed bag of volatility, and it really is category by category. And so there are number of areas, and silicone is a key one, where we have been dealing with multiple price increases across a 12-month period, and we're continuing to try and manage that.

Operator

And we have Frank Mitsch on the line.

Frank Mitsch - *Fermium Research - Senior Managing Director*

Obviously, the November 28 Investor Day, I thought, went very well. And you guys laid out a pretty good MAP to Growth. It happened late in the quarter, during -- a bit late in the fiscal second quarter, and obviously, a bit of earnings miss here, I was wondering, was there anything that happened late in the quarter or after the quarter closed that may have negatively impacted the results, such that you guys came in lighter than where consensus was?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

No I'll tell you two things that I think, one was a mistake in our part; and the other was something that we didn't anticipate and maybe should have. The mistake on our part was, when we're looking at the volatility of this year relative to all of the changes that were coming and all of the related charges, we decided not to provide guidance. And in hindsight, the second-quarter consensus was up 17% or 18%, and that's not -- it hasn't been in the cards for us or anyone else, and it was not part of our internal plan. The reason we decided to provide specific guidance for the third quarter was that very reason. Again, I think that simple math would suggest that there was going to be a $10 million or $12 million turnaround in tax expense year-over-year, and so a couple other items like that.

The second item was the accounting change in -- now a requirement that if you have a marketable securities portfolio, apparently much like banks, you have to mark-to-market every quarter the equity portion of that. And it was a nonevent the first quarter for us, I think it was a $1 million pretax gain.

100% of the shortfall EPS-wise from last year to this year could be attributed to what was almost a $10 million reversal where we had $3.5 million of gains last year, this is in our captive insurance portfolios, and this year, I think we took a six-or-so-million-dollar hit. And that will be a challenge that we communicate better in the third quarter. It is a nonoperating item. We went through this in '08 and '09, and had six quarters of impairments, and then as most of you would know, by the end of '12 or '13, we have recovered more than had been written off in impairments in terms of the market recovery. Just to give some color on that, our captive insurance companies had been a very smart way for us to manage certain levels of insurance. Our total portfolio, is about $130 million, $93 million of that is equity. This mark-to-market has a component to what that is. Historically, you would only record realized gains or losses. In this case, you mark-to-market, but if it's actually not a realized gain or loss, there's no tax consequences. And so, we'll hide that off and explain that and separate that from our market issues. That item alone is the EPS reason why we're below last year, and so hopefully, that answers your question. I think it was, in hindsight, for a couple of reasons, maybe a mistake not to provide guidance. We certainly would've guided people differently in the second quarter, and I think looking at us, looking at our peers, I think that makes sense. And with the numbers out in the third quarter and the progress that we're making in our MAP to Growth initiative, we're making good progress, and we actually feel good about what's coming. And there's nothing that's happened in the second quarter or will happen in the third quarter that makes us change our projections as outlined in November 28.

Frank Mitsch - *Fermium Research - Senior Managing Director*

That's extremely helpful. And there was a lot of commentary regarding the negative weather impact, and you'd indicated that you thought that was kind of a temporary sort of impact. So, should we be thinking about kind of a recovery in that regard as a fiscal fourth-quarter event when the spring comes around and we make up for some pent up demand? Is that how you're thing about that?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

There's a couple areas of possible upside, if you will. We've been dealing with weather issues in our consumer segment for most of last year. It's not been unique to us, it's not been a very good painting year. I suspect that the wet fall will highlight that for other folks in the exterior painting categories. I think there's pent up demand in a lot of the consumer businesses and so if we have a reasonable spring, you'll see that. I think there's continued strong growth potential in the Tremco Roofing restoration coatings. We've got a good backlog there. And so, it'd be nice to see that upside. Time will tell. But there's been every indication in terms of our construction products, our roofing products, the Dryvit systems and a lot of our consumer products that some of the negative impacts have been weather-related and temporary.

Operator

From Baird, we have Ghansham Panjabi.

Ghansham Panjabi - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

I guess, going back to Frank Mitsch's sort of question as well, on industrial, and sticking to the overseas market, what exactly are you seeing in Europe? Was Europe actually down year over year in the quarter from a volume standpoint? Can you give us a sense as to how the other regions did? And then just given some of the weakness in energy prices and your exposure there, should we expect a sequential deceleration in industrial? Or do you think that would be offset with some of the recovery from weather?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. So, excluding acquisitions, Europe was flat, and in our industrial segment, that was disappointing. Latin America continues to be challenged as well. And so, regionally, those are the two most significant areas for us outside of North America. North America continued to be pretty solid. And as I highlighted earlier, obviously, there's some real strong elements of organic growth that helps drive organic growth through the whole segment of about 3%. We don't see a lot of strength in Europe right now, and so I don't think there's any big disaster, but it's not going to be a driver of improved performance in the second half of the year as far as we could tell, other than the things that we would drive relative to our MAP to Growth program.

Ghansham Panjabi - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Got it. And then just my second question, kind of going back to raw materials and pricing, did price-cost -- just purely focusing on price-cost, did that come in where you thought it would during the second quarter relative to your initial expectations? And then what is reasonable from our vantage point to kind of think about year-over-year margin parity for your businesses on a consolidated basis?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

So I think we're making the headway in terms of raw material costs and price increases in our industrial segment and our specialty segment. That's not been true in our consumer segment. I mentioned silicone, that's a big part of it, but it's been a certain other packaging categories. So, our consumer segment is more tilted towards categories like silicone and others that have not eased up, and also are more packaging-intensive because there's more units. But we're continuing to make good progress there and we would expect to make progress across the entirety of our consumer segment customer base by this spring. And that, as I mentioned earlier, is in part in relationship to some line review wins we had last year, which came along with some commitments on price that are now annualizing. I think that we're starting to see raw materials ease and we're starting to see the benefits of our structural changes, and we'll be in a better position in April to tell you what those are. They will show up in our results somewhat later than they will in some of our larger competitors because of the difference between FIFO and LIFO accounting. But we'll also be able to provide more data because we have better and more accurate data at our fingertips today, certainly at my level, than we've had in the past.

Operator

From RBC Capital Markets, we have Arun Viswanathan.

Arun Viswanathan - *RBC Capital Markets, LLC, Research Division - Analyst*

Just wanted to understand, I guess on industrial, I guess relative to your expectations, did those results kind of come in where you guys expected them? Or was there some extra softness? And I'm also curious just on the margin front, was there some extra cost that you potentially incurred that hurt those margins?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

I think the disappointment in our industrial was related to more on the revenue side, some of the weather-related items that we talked about, as well as flat results in Europe. Fifty percent of our industrial segment is outside of North America and we did not experience growth there. And so that was a challenge for us. We are making good progress on the margin side. And I think that will show up in the coming quarters. That's certainly -- the FX also negatively impacted us both on translational and in certain places, transactional perspective, and again, our largest exposure internationally is in our industrial segment.

Arun Viswanathan - *RBC Capital Markets, LLC, Research Division - Analyst*

And then just two quick follow-ups. So first off, the tax rate, just wanted to understand, do you expect to see that 26% rate from here on? My apologies if I missed that.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

That's correct. In the third and fourth quarter, that's about where we would see taxes.

Arun Viswanathan - *RBC Capital Markets, LLC, Research Division - Analyst*

Okay, great. And secondly, at the Investor Day, you talked about kind of maintaining a level of sales growth that's required for that 540-basis points of margin improvement. Do you still see that as relatively achievable? Or was there potentially some greater slowing that would cause you to potentially adjust that view, that growth maybe, could be a little bit below where you thought it would be that and that would result in less margin improvement?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

For the things that we control, we see that as relatively achievable, and in fact, in the quarter, we did. I think between organic growth and acquisitions, we're in the 5.5% or 6% range. Foreign exchange negatively impacted that by two points. Who knows where that will go. The dollar seems to be weakening as we speak today. But the direction of the dollar and the stock market are anybody's guess in the coming months and quarters. But we feel pretty good about our ability to generate, through a combination of organic growth, by keeping our nose to the grindstone and our sales and marketing people focused on the market and our customers, as well as the regular stream of acquisition activity that we see as possible, that those targets are very doable. The foreign exchange swings, plus or minus, will be a variable that we don't control, but I think, over time, we wouldn't expect them to be meaningful. But time will tell.

Operator

From Vertical Research partners, we have Kevin McCarthy.

Kevin McCarthy - *Vertical Research Partners, LLC - Partner*

A couple of questions, as you've reinstated earnings guidance, as I look at the range for the fiscal third quarter and irrespective of the level of the guidance, I guess I'm impressed that you have a very narrow range of just $0.02 from top to bottom. Can you comment on the level of your visibility at this point as you move through the MAP to Growth execution? And if it turns out several months from now that your earnings are materially better or materially worse than what you're laying out as guidance, what are some of the key variables that might be harder to predict right now that could be a swing factor with regard to your near-term earnings?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

So I think the -- great question, the variables will be revenues, and some of that -- people would be tired of this, but some of that will be weather-related. So far, we seem to be in pretty good shape there. And certainly, the foreign exchange will be a variable that we don't control. So, we'll see where that goes; it seems to be settling down a little bit. And then the third variable, which, again, I mentioned, I think we will figure out how to carve out so that it's obvious as to what the impact is, but also separate it from our core operating results as this mark-to-market. Last year, I think we had $3.5 million gains on a pretax basis in the third quarter.

Russell L. Gordon - *RPM International Inc. - VP & CFO*

More like $5.5 million.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

More like $5.5 million. And this year, we'll end up certainly with some level of millions of dollars of losses if the market stays where it is. So, there could be a material swing there. That's a nonoperating item that we will be sure to specifically address. Those are the variables. You separate that and I think the variables are really revenues, and weather makes a difference in the third quarter, particularly in our consumer segment. If you get an early spring, a lot of times, we'll get strong shipments particularly after the January year end, so a lot of our big accounts in February, and a big February in consumer can make a big third quarter. A weak February consumer means this all gets pushed into the fourth quarter. So, that's the biggest variable I would see in revenues and where it might come from, and then the other's FX. I think we have expenses pinned down very well, and I think we're continuing to generate a growing level of restructuring savings that we're pretty confident in.

Kevin McCarthy - *Vertical Research Partners, LLC - Partner*

That's really helpful. And with regard to the weather impact, have you quantified or attempted to quantify the aggregate impact in the fiscal second quarter? And how that might have split between industrial and consumer?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

I don't have that off the top of my head, Kevin, other than knowing that we had disappointing results in the three businesses I mentioned: Tremco Roofing, Dryvit and some of our consumer product categories that are exterior-use products. And we believe those shortfalls to our internal plan were related to weather.

Kevin McCarthy - *Vertical Research Partners, LLC - Partner*

And then last one, if I may, just coming back to guidance. Do you feel as though, looking ahead to the May quarter, that you would be in a position to compare positively on a year-over-year basis on the bottom line?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Yes.

Operator

From Morgan Stanley, we have Vincent Andrews.

Vincent Andrews - *Morgan Stanley, Research Division - MD*

So actually I'd just like to follow up on that fourth-quarter question, just in terms of -- and I appreciate the comments, Frank, about guidance and obviously, we were all, including myself, ahead of things for 2Q and now probably 3Q. Does that extend to 4Q? It would seem logical that you got 2Q wrong and 3Q wrong and probably 4Q wrong as well. So, I'm just kind of asking more specifically about your comfort with the actual consensus number for the fourth quarter?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Yes, I don't think we're in a position to provide guidance for the fourth quarter now. I think on the April call, we will provide the same type of specific guidance then on the fourth quarter that we have provided in the third quarter. And then I think we will be in a better position as we look into next year to provide some more reasonable guidance. As I've mentioned, in hindsight, it seems like the right thing to do, given all the variabilities and all the restructuring charges that we would have and not knowing the timing of that. But certainly, in hindsight, it did not help us to not be providing some high level of guidance. And so, I think it was as much a communication hiccup relative to the second quarter and third quarter. Certainly some of it's performance-related, but a lot of it's math around tax issues last year versus where we'll be this year in the third quarter and expectations on guidance that were never part of what was happening in our industry or what we saw for the year, and that was our mistake in communications, and we will improve.

Vincent Andrews - *Morgan Stanley, Research Division - MD*

Fair enough. And I appreciate the candor on that. Just a couple of other follow-ups. The wet weather, was that primarily a September issue with the hurricanes or was that actually an October and November issue as well?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

It was the wettest record on fall -- or fall on record -- or the second wettest fall on record, and it was a great frustration relative to -- we've mentioned Tremco Roofing a number of times, we've got good backlog and good order flow and a lot of projects that were delayed or put off or interrupted specifically. And it was just a frustrating period of time. The same is true for our Dryvit business, which is all exterior work and it's more anecdotal in terms of measuring what we thought would happen versus consumer takeaway in certain categories that, again, are more exterior related.

Vincent Andrews - *Morgan Stanley, Research Division - MD*

Okay, and maybe just one last quick one. If you could just tell us roughly what you think the FX headwind will be in the third quarter and fourth quarter, that would be helpful.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Yes, it's hard to say. It was two percentage point of sales in Q2. I would hope it would be a little bit less than that, but I think that's probably a number at this point you can count on. That's what I would stick in the model. I'll say that and the dollar's starting to weaken a little bit relative to Fed easing off on further rate increases, and so -- but 2% is probably what I would expect, and depending on where things go, maybe it won't be quite as negative.

Operator

From KeyBanc, we have Mike Sison.

Michael Sison - *KeyBanc Capital Markets Inc., Research Division - MD & Equity Research Analyst*

Frank, when you think about the fourth quarter, I know you don't want to give specific guidance, but can you maybe talk about some of the year-over-year positives that you'll see as tailwinds for the fourth quarter in terms of earnings growth?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. So, I think the fourth quarter will be the first period where some meaningful MAP to Growth savings will start to be realized. We announced five plant closures in this quarter, and as I commented on earlier, in some cases, we have WARN Act requirements, in other cases, it's just an internal announcement that, obviously, once we've announced something internally, it can quickly go external. So, we feel comfortable in communicating those. But in many instances, the operations aren't ceased for 60 or 90 days, and at that point, you're starting to save the dollars. The negotiations that we have been having with a lot of our key vendors in terms of volume consolidation and some improvements and pricing in terms, have trigger dates of the end of January, end of February. Obviously, there's more work to do there. But so, we feel good about having some meaningful benefits in the fourth quarter. I think secondly, last year was a very disappointing quarter in our consumer segment for a number of reasons. There was a lot of competitive activity and some different changes in the marketplace. That all shook out positively for us in terms of market share gains as we got into the early summer months. And so, I think that will reflect positively on our results in the fourth quarter as well. I think those are the principal categories that we see as driving what will be a year-over-year positive fourth quarter.

Michael Sison - *KeyBanc Capital Markets Inc., Research Division - MD & Equity Research Analyst*

Great. And then just one quick follow-up. You talked about acquisitions as still a core focus for RPM. Any update on the environment? Any areas that you think you're going to be particularly focused on in acquiring over the next couple of quarters?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

We completed, in this last quarter, another cleaning category product for Rust-Oleum, Mold Control, and that's a pretty exciting category for Rust-Oleum in terms of growth. We completed this year a relatively small product line focused on railcar called Strathmore with Carboline, and that's turning into a real nice acquisition. There are smaller deals, but particularly on the industrial side, if we can start to mirror what we've done in consumer, we picked up a nice product line and some good technology that's focused on a particular area, and we've expanded what was a sales force of a dozen people into the pockets of a Carboline sales force of 200 people and that's really driving revenues. And so, we're looking for more deals like that. I don't expect our deal flow to be any bigger than what we communicated in November 28, which is somewhere in the $150 million to $200 million a year, made up of multiple deals. But the deal flow out there is still pretty solid and we're working hard to find more opportunities like that.

Operator

From Seaport Global Securities, we have Mike Harrison.

Michael Harrison - *Seaport Global Securities LLC, Research Division - MD & Senior Chemicals Analyst*

Kind of sticking with the acquisition theme. You did mention Nudura there, but it looks like the contribution from Nudura was pretty solid in the quarter. I know that, that's a complement to Dryvit, but I'm guessing it does not have the exterior -- the weather-related impacts that Dryvit saw. So, can you just talk a little bit about the performance of Nudura in the quarter and maybe help us understand the revenue potential relative to that $40 million annual contribution you mentioned when you acquired that business?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. That was the revenue base. We're very excited about Nudura. When you look at the durability, particularly as there are concerns around weather-related events and if you look at code changes in relationship to the energy efficiency of the insulated concrete form structure that Nudura has, we're big, we're long on Nudura, we're very bullish about it. There are good synergy opportunities within Dryvit and there are also good synergy opportunities with the Tremco Sealants part of our construction products group. And as we get into what is typically our March growth and strategy, the real challenge for us is to be -- is to think about how and how much and where we can be most effective in promoting Nudura to a larger audience. It is one of the building category elements of the future that we believe in. And we just got to get out there and promote it and get it specified in greater areas, in greater amounts. But a very exciting opportunity and a great fit with our multiple RPM product areas.

Michael Harrison - *Seaport Global Securities LLC, Research Division - MD & Senior Chemicals Analyst*

All right. And then you mentioned increasing the advertising spend within the consumer business. It seems like consumer had kind of the biggest margin shortfall, at least relative to my expectations. A lot that was also raw material, but just wondering how much the additional advertising spend was maybe weighing on the margin and consumer on a year-over-year basis?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Yes, I don't know if it is a big difference. It's up in the quarter, about $2 million and...

Russell L. Gordon - *RPM International Inc. - VP & CFO*

$200,000.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

No, $200,000. So, what was up in the quarter, only $200,000 year-over-year, and it's up a couple million dollars on the year. But it's a category that, in light of a focus on cost improvement and restructuring, that we're not cutting. In fact, in certain areas, we're promoting. And I think we have to do that, particularly in light of what's been disappointing consumer takeaway, a lot of it, we believe, is weather-related. But as we get into the spring as well, we need to continue as a leader in a lot of these categories to promote the use and work with our major customers to get people in the stores and get people moving in these categories. So, that's an area that we have deliberately not cut, and are focused on. Obviously, Rusty corrected me, it was up $200,000 in the quarter, so that's not a big number this quarter.

Michael Harrison - *Seaport Global Securities LLC, Research Division - MD & Senior Chemicals Analyst*

Got it. And then quick one for Rusty. Just in terms of the diluted share count around the end of the quarter, I know you didn't redeem that convertible bond until the end of the quarter. But it looks like, for accounting purposes, that convertible was excluded from the share count for the entire quarter. Is that correct?

Russell L. Gordon - *RPM International Inc. - VP & CFO*

Yes. For the GAAP set of financial statements, we're on the two-class method. And the two-class method has a lower share count because we're not including unvested equity awards in the share count. And then on the non-GAAP set of numbers -- the as-adjusted set of numbers, with the as-adjusted EPS, at $0.52, -- we're using a higher share count because were using the treasury method for shares and that does include the shares from the convert. We're going to see the benefit of the convertible redemption in future quarters, but we did not get it so much in the second quarter because we redeemed it three days before quarter end.

Michael Harrison - *Seaport Global Securities LLC, Research Division - MD & Senior Chemicals Analyst*

So, maybe a better way to ask the question is what was the diluted share count at the end of the quarter that we should be using for Q3?

Russell L. Gordon - *RPM International Inc. - VP & CFO*

Yes. In terms of the share count for Q3, it will be down about 3.3 million shares for the impact of the convertible. So, it would be down in the $133 million range for the quarter. And then, on an annualized basis, we should pick up $0.03 to $0.04.

Operator

From Northcoast Research, we have Kevin Hocevar.

Kevin Hocevar - *Northcoast Research Partners, LLC - VP & Equity Research Analyst*

On the pricing agreements that you -- discussions you've had, it sounds like you locked in pricing for February, March timeframe. Is that across all the segments is it focused -- it sounds like maybe in consumer to some degree, just wondering if you could give some clarity on where the pricing's being realized?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Sure. The pricing in our consumer and specialty products has been happening throughout the year. We did have some price increases in our consumer businesses earlier in the year, and across much of our customer base. But in certain areas where we had significant competitive line reviews a year ago and/or new product categories as part of our commitments, we were locked in for a 12-month period. And those lock-in periods are expiring this spring.

Kevin Hocevar - *Northcoast Research Partners, LLC - VP & Equity Research Analyst*

Got you. And just the $10 to $0.12 EPS, I just want to make sure, is that a non-GAAP number that excludes all the MAP to Growth and other restructuring charges?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Yes. That is exclusive of the -- whatever the charges will be in the third quarter. And again, we'll highlight that in detail, obviously, when we report the quarter.

Operator

From JPMorgan, we have Jeff Zekauskas.

Jeffrey Zekauskas - *JP Morgan Chase & Co, Research Division - Senior Analyst*

Your cash flow has improved for the six months by about $30 million, but your deferred tax, there was a positive change in deferred taxes of about $30 million for the six months year over year. And there was also an $11 million positive swing in realized and unrealized marketable securities cash flow. Can you discuss what those are for the year? Are these permanent or impermanent? And what's driving the changes in deferred taxes in particular?

Russell L. Gordon - *RPM International Inc. - VP & CFO*

Sure. Last year, Jeff, you're seeing a big number on the deferred tax line on the cash flow, a use of cash of $32 million, and that's really an adjustment to the net income line up above for some nontax impact of our, what I would call our legal entity realignment project last year, which allowed us to get some big tax benefits in the second quarter and our tax rate, you might remember in the second quarter last year, it was only 12% because of this project. So, that's impacted by that specific item where we basically were able to flip a large amount of our APB 23 reserve as a result of improved utilization of foreign tax credits that resulted from that. Your next question was on the marketable securities line, and we are showing this year a change in that. We have proceeds from sales of marketable securities this year of $35 million. That was actually cash we've been able to move from our captive insurance companies, which Frank mentioned before, for use in our operations, because our captives were a bit overcapitalized and as a result, we're able to get a net positive cash flow. If you look at the prior year on the marketable securities lines, that's more normal activity each quarter as we rebalance our investment portfolio.

Jeffrey Zekauskas - *JP Morgan Chase & Co, Research Division - Senior Analyst*

So the tax rate that you're now talking about of 26% for the third quarter, like, in theory, why shouldn't your tax rate be closer to 21%, plus or minus a little bit? And is that a more reasonable forecast for 2019? Your tax rate, I think, was 28% in this quarter. I don't understand why it's so high.

Russell L. Gordon - *RPM International Inc. - VP & CFO*

Yes, the 21% is actually the U.S. statutory rate.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

It's a combination of jurisdictional mix, and now, for the first time ever with the U.S. tax rate meaningfully favorably better than most foreign operations. The jurisdictional mix will likely, quarter by quarter, be higher because of the 1/3 of our business-or-so that is outside of the United States. So unlike past years for us or in other companies where you would end up with an actual tax rate somewhat below the U.S. statutory rate, which was at least in the developed world, the highest in the world. Now you're likely to see a higher tax rate.

Russell L. Gordon - *RPM International Inc. - VP & CFO*

And also, we have state taxes, included on top of the Federal of 21.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

But the biggest part of it's jurisdictional, and now we tend to average up our tax rates because of our foreign income at higher tax rates than where the U.S. is. So, that's the benefit of tax reform that I think we're all enjoying.

Jeffrey Zekauskas - *JP Morgan Chase & Co, Research Division - Senior Analyst*

What are your high tax rate jurisdictions?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

I can't answer that off the top of my head right now. But I can tell you, it's almost every country in which we do business outside of the United States in the developing world.

Operator

From Great Lakes review, we have a follow-up from Jason Rodgers.

Jason Rodgers - *Great Lakes Review - VP*

Appreciate you taking the follow-up, I just had a quick one for Rusty. If the diluted share count was 131.7 million in the second quarter and that did not include the 3.3 million share reduction from the convertible, then why should the share count be around 133 million in the third?

Russell L. Gordon - *RPM International Inc. - VP & CFO*

Yes. We don't know the third for sure because we could either use the two-class method or the treasury method. It depends on earnings. We've picked the one, Kristine, that's most antidilutive, right? So, that would depend on what earnings are during the third quarter. So, the third quarter is a bit uncertain just due to the nature of the season and we're at a low earnings point. We're not sure which method exactly we'll be on. But we could tell you for sure we've redeemed those shares, and there's 3.3 million shares that used to be in our diluted share count under the treasury method that aren't there.

Operator

From Gabelli & Company, we have a follow-up from Rosemarie Morbelli.

Rosemarie Pitras-Morbelli - *G. Research, LLC - Research Analyst*

This is for Rusty. As long as there is so much volatility regarding the mark-to-market of the securities of your portfolio, why not is it at all possible to take it out of the adjusted numbers? So, we look at operations on an apples-to-apples basis, eliminating the volatility of that item?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

We will work with our auditors to address that in the third quarter. And certainly, that's what we aspire, to. So, as a nonoperating item, it will be pluses and minuses, and so we need to work on how we would do that and then just make it a permanent adjustment and carve it out of our operating results.

Rosemarie Pitras-Morbelli - *G. Research, LLC - Research Analyst*

Okay. And if we look at the second quarter, what was the impact of that item on a per share basis? I'm assuming it has the tax impact on it, and I have no idea what the rate is, I am assuming it's not your corporate rate.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

It is $0.05 from the quarter. That's why I mentioned that item alone was the difference between being flat year-over-year on the EPS line. And the aggravating part of that accounting reg is, again, in the past, you would only recognize the gain or loss if they were realized as you manage your captive insurance companies to -- where you would have to liquidate the insurance needs and things like that or offset gains and losses. Now you'll mark-to-market, but because they're not realized, they're not tax-deductible. And so, if you have an unrealized $5 million hit, it's not actually tax-deductible until you effectively sell those securities and have an actually realized loss. So, it's a really double whammy in terms of your bottom line. So again, we're going to work to figure out the appropriate way to address it and then carve it out of our results in future periods.

Rosemarie Pitras-Morbelli - *G. Research, LLC - Research Analyst*

So just making sure I get this properly, instead of $0.52, then you would have reported $0.57 from operations adjusted in the second quarter?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

I think that's the simplistic way of looking at it. I think that's right.

Rosemarie Pitras-Morbelli - *G. Research, LLC - Research Analyst*

Yes, I like simple. And looking at the third quarter, in that $0.10 to $0.12, do you have some kind of an impact from that particular item incorporated in those numbers?

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Yes, we have about a $5 million negative impact on a year-over-year basis in those items between the gains we realized in the prior year and an anticipated loss this year. But we won't know the actual number until we closed the quarter and whether the stock market between now and the end of the quarter is up 1,000 points or down 1,000 points or somewhere in between.

Operator

Thank you. We will now turn it back to Frank Sullivan for closing remarks.

Frank C. Sullivan - *RPM International Inc. - Chairman, President & CEO*

Thank you, Brandon. Thank you very much for your participation in our call today. I'd also like to thank the RPM associates around the world who are continuing to generate solid growth in a challenging environment. Most importantly, we appreciate your questions and your commitment as we continue to execute our 2020 MAP to Growth and drive a more valuable and more competitive RPM.

Thank you. Happy new year to all, and we will look forward to talking to many of you in the coming months and updating everybody on our progress on our April investor call. Thanks, happy new year, and have a great day.

Operator

Thank you. Ladies and gentlemen, this includes today's conference. Thank you for joining. You may now disconnect.