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WAIR - Q4 2016 Wesco Aircraft Holdings Inc Earnings Call

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PRESENTATION

Operator

Welcome to the Wesco Aircraft Holdings fourth-quarter and FY16 conference call. My name is Anna, and I will be your operator for today's call.

(Operator Instructions)

Please note that this conference is being recorded. I will now turn the call over to Jeff Misakian. Please go ahead.

Jeff Misakian - *Wesco Aircraft Holdings Inc. - VP of IR*

Thank you, Anna. Good afternoon, everyone, and thank you for participating in Wesco Aircraft's FY16 fourth-quarter and full-year earnings call and webcast. We've included slides with today's presentation to help illustrate some of the points being made and discussed during the call. These slides can be accessed by visiting our website at www.WescoAir.com and clicking on Investor Relations. We are joined today by Dave Castagnola, President and Chief Executive Officer; and Rick Weller, Executive Vice President and Chief Financial Officer.

Please turn to slide 2. As a reminder, today's conference call includes forward-looking statements within the meaning of federal securities regulations. Although the Company believes that such forward-looking statements are reasonable, we cannot assure you that any forward-looking statements will prove to be correct. Forward-looking statements are not guarantees of future performance, and involve known and unknown risks, uncertainties and other factors which may cause actual results to differ materially from those anticipated at the time the forward-looking statements are made.

Additional information relating to factors that may cause actual results to differ from our forward-looking statements can be found in the Company's filings with the Securities and Exchange Commission, including the Company's annual report on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K. Wesco Aircraft undertakes no obligation to update or revise forward-looking statements except as required by law. Now I would like to turn the call over to Dave Castagnola. Dave?

Dave Castagnola - *Wesco Aircraft Holdings Inc. - President & CEO*

Thanks, Jeff. Good afternoon, everyone. Turn to slide 3. FY16 has been a year of improvement and transformational change for Wesco as we restructure the Company to best reflect our position as a full-scale supply chain service provider. These transformational activities have delivered results at a better pace compared to Wesco recent history, and provide an improving foundation for FY17, which we'll cover later in our remarks.

Wesco came into FY16 faced with declining sales, slow sales momentum from our larger customers, high SG&A costs, delivery performance challenges, and a supply chain approach reflecting procurement practices that were in line with the smaller, more traditional distributor. During FY16, our large-customer sales improved faster than we anticipated, while the ad hoc market was softer, influenced by major OEM inventory adjustments on certain wide-body programs, and as evidenced by distributors slowing down purchases. At the same time, the impact of currency was greater than we had anticipated, particularly the British pound. Both sales mix and currency affected Wesco sales and margin performance relative to our goals in FY16.

We took several actions to address these issues in the fourth quarter. However, the pound declined at a much faster rate than in previous periods. And while ad hoc sales had improved in the third quarter, the final three months of the year were more in line with the first half of FY16. As we've discussed in previous periods, ad hoc sales can fluctuate from one quarter to the next, making them challenging to forecast.

We also increased investment in the fourth quarter in new business implementations required to support sales growth that Wesco had secured throughout FY16. Last quarter, we talked about the establishment of an implementation team, which has initiated multiple implementations at customer sites around the world. This is on a larger scale compared with past Wesco experience, and the team is making good progress.

Please turn to slide 4. The Wesco team tackled these challenges and met or exceeded many of our FY16 goals. We recorded low single-digit constant currency sales growth, reduced expenses by $32 million, which included $6 million of favorable currency impact, and achieved 113% free cash flow conversion. Adjusted EBITDA margin improved 50 basis points in FY16, the first expansion in margin in many years.

We achieved this expansion in spite of the combined negative impact of 30 basis points of currency movements and the investment in new business implementations I just mentioned. SG&A cost reductions primarily delivered the EBITDA margin improvement. The progress made in FY16 allows us to enter FY17 with stronger contract sales momentum, an improved cost structure, and a solid balance sheet. I will talk more about our FY17 outlook at the end of our remarks.

Next, I will provide you with an overview of our fourth-quarter performance. Please turn to slide 5. We reported net sales of $367 million, operating income of $40 million, and adjusted diluted earnings per share of $0.30 in the FY16 fourth quarter. Fourth-quarter sales increased 2% on a constant currency basis, reflecting momentum in long-term contracts. We booked major new business wins, expanded work scope and renewed contracts with existing customers. I will talk more about sales performance in FY16 in a moment.

We also continued to reduce costs, which drove higher operating and net income. Through working capital management and stronger earnings, we generated free cash flow of $48 million, which allowed us to make debt repayments of $35 million. We also refinanced long-term debt in October, improving our credit profile.

Please turn to slide 6. Growth in long-term contracts continued to be the primary driver of higher sales in the quarter. Contract sales rose at a mid single-digit pace, reflecting increased customer production, new wins and expanded scope. This was partially offset by a mid single-digit decline in ad hoc sales.

The pace of new wins and expansion was strong last year, reflecting recognition of the value in our broad portfolio of hardware and chemical products and supply-chain management services, as well as an expanding presence in the aftermarket. In FY16, Wesco sales team won new business with large commercial and defense companies, and continued the conversion in growth in long-term agreements, while also successfully renewing business with other large customers at a retention rate in the high-90% range.

New business wins and renewals during the year included major long-term agreements with Triumph, GKN and Gulfstream, and in October we announced multiple contracts with UTC. We also renewed a major chemical management services contract with a large defense OEM, and announced in early November a renewed contract to perform chemical management services with SAIC at military depots across North America. The new wins and the scope expansion are expected to generate annual sales that will support Wesco's improved growth in FY17.

As you know, the timing of this growth depends on several factors, including customer needs, new product lead times, inventory transition balancing, implementation schedules and customer supply chain maturity. In many cases, contracts can take up to a year to implement, and two years to fully realize their annual value. However, it is encouraging to note that we enter FY17 with sales momentum and an expanding pipeline of opportunities.

With our MRO customers, increasing content wins this year included multiple agreements to provide products and services with airlines and MRO service providers globally. We continue to grow our MRO sales resources, and I'm pleased with the progress we're making.

Please turn to slide 7. Supply-chain management initiatives made good progress this year, as we focused actions in line with ordering that supports demand from our larger customer contracts. As a result, we matured delivery management processes with our suppliers. We also have improved supplier delivery performance, improving visibility through the use of metrics, order-book alignment and prioritization, a daily cadence of interaction, on-site reviews with action plans, and capacity assessments.

Wesco advanced the implementation of sales, inventory and operations planning, or SIOP, aligning ordering practices to forecasted demand, and increased the number of long-term agreements with suppliers. We have brought our ordering practices with our partners more in line with those of large aerospace OEMs, while improving efficiencies in our material acquisition processes. Our SIOP process aligns our major market channels and long-term forecasts, giving us visibility and control of material receipts and payment disbursements. As a result, we've seen improvements in inventory and cash management timing and predictability as the year progressed.

Please turn to slide 8. We executed operational initiatives, achieving our site and supply goals for the year. Our streamlined network began showing results, with delivery performance at our major hubs improving service to our customers. Restructuring actions in the fourth quarter of last year delivered efficiencies in operations and expense reductions for Wesco in FY16, and overall, improved our cost structure, which was leveraged to provide EBITDA margin improvement.

We remain focused on continuous improvement to drive logistics flow and delivery performance. Our SIOP process is helping us drive standard work throughout the network, improve the way we manage customer bin replenishment globally, increase cross-dock flow for same-day shipments, and establish a more efficient network to manage and leverage an increasing volume in new business. Rick will now provide a more detailed discussion of our fourth-quarter and FY16 results, and I will follow this with our FY17 outlook and some closing remarks. Rick?

Rick Weller - *Wesco Aircraft Holdings Inc. - EVP & CFO*

Thanks, Dave. Please turn to slide 9. Net sales in the FY16 fourth quarter of $365.6 million decreased 1% compared to the same period last year. Foreign currency movements had a negative impact of approximately $12 million on FY16 fourth-quarter sales -- two times the level we experienced in previous quarters this fiscal year.

Constant currency sales were up 2% compared to the same period last year, led by mid single-digit contract growth supporting major commercial and military customers. Growth was similar at hardware and chemicals. Ad hoc sales were down at a mid single-digit rate year over year on a constant currency basis.

Please turn to slide 10. We further reduced SG&A, which drove income from operations of $40.3 million and net income of $23.3 million, or $0.24 per diluted share, in the FY16 fourth quarter. The operating and net income figures compare to an operating loss of $326.2 million, and a net loss of $214 million, or $2.21 per diluted share, in the fourth quarter of FY15. The loss recorded in last year's fourth quarter was primarily due to several actions taken to position the Company for stronger performance, including goodwill impairment of $263.8 million, and inventory adjustments of $91.3 million.

For comparison purposes, the remainder of my remarks will focus on results that exclude adjustments and charges, where applicable. We have provided a reconciliation of these non-GAAP to GAAP results in the tables that accompany our press release and in the appendix to the earnings call slides.

Income from operations of $40.3 million in the FY16 fourth quarter represents a 39% improvement over adjusted operating income of $28.9 million in last year's fourth quarter. Operating margin was 11% in the fourth quarter of FY16, compared to an adjusted operating margin of 7.8% in the same period last year.

SG&A as a percentage of net sales was 15.1% in the FY16 fourth quarter, 340 basis points lower than last year's fourth quarter, primarily due to a decline in people-related costs, currency and professional fees. SG&A decreased $32.2 million in FY16, above our target range for the year. Currency movements contributed $5.6 million of the decline. On a constant currency basis, SG&A was $26.6 million lower in FY16, meeting our goal of $25 million to $30 million.

Gross margin was 30 basis points lower in the FY16 fourth quarter, compared to an adjusted gross margin in the same period last year, primarily due to a 120-basis point impact from currency movements, partially offset by a better product mix of 50 basis points, and inventory adjustments of 40 basis points.

Adjusted net income was $29.9 million or $0.30 per diluted share in the FY16 fourth quarter, compared to $26.5 million or $0.27 per diluted share in the same period last year. Adjusted net income reflects the items that drove operating profit in the quarter, offset by the decline in nonrecurring items mentioned earlier, and a decrease in other income net.

Other income declined by $3.4 million, primarily due to a gain of $2.7 million in last year's fourth quarter related to transactions that were denominated in currencies other than the functional currency of the reporting subsidiaries, primarily the British pound. Transactional currency impact is related to timing differences that arise when net assets are booked and settled, primarily receivables and payables.

We substantially hedged our pound exposure to movements in foreign currency in the FY16 fourth quarter. As a result, there was minimal transactional currency impact in the quarter. However, currency movements resulted in a negative translational impact of approximately $1.9 million in net income. The transitional impact results when functional sales and costs, again primarily those in the British pound, are translated to US dollars at lower exchange rates.

As we mentioned last quarter, Wesco is establishing a new UK legal entity that combines legacy hardware and chemical entities. As a SIOP supply initiative, this will allow for operational efficiency, leverage, and improved customer service across multiple commodities. The appropriate functional currency for the new entity is under review and will be determined prior to its establishment, which is expected to occur in the middle of FY17.

Our effective tax rate in the FY16 fourth quarter was reduced by a favorable mix of taxable income across jurisdictions, and discreet tax items. We expect our effective tax rate for FY17 to be in the range of 28% to 30%, primarily due to projected mix of taxable income across jurisdictions, and lower discrete tax items.

Adjusted EBITDA was $49.6 million or 13.6% of net sales in the FY16 fourth quarter. This compares with $46 million or 12.4% of net sales in the same quarter last year. Adjusted EBITDA margin also reflects the improvement in operating income and the negative impact from foreign currency movements that I just described.

Please turn to slide 11. Sales in North America were down 1% in the fourth quarter, primarily due to a decline in ad hoc, partially offset by higher contract sales. Contract sales reflect increased production, new business wins, and scope expansion for commercial and defense customers.

Operating income in North America was $27 million or 9.2% of net sales in the fourth quarter. This compares with adjusted operating income of $24 million or 8% of net sales in the same period last year. Operating income and margin were higher, primarily due to lower SG&A expense, offset by a decline in gross profit. Gross margin was impacted by the mix of ad hoc and contract sales. SG&A expenses reflect lower people-related costs and professional fees.

Turn to slide 12. Sales in the Rest of the World segment declined 1% in the fourth quarter, but were up approximately 16% on a constant currency basis, with increases in both ad hoc and contract sales. Operating income in the Rest of World was $13.2 million in the fourth quarter, or 18.8% of net sales, compared with adjusted operating income of $4.9 million or 6.9% of net sales in the same period last year. Higher operating income and margin in Rest of World primarily reflects an increase in sales volumes and mix.

Please turn to slide 13. Net inventory increased $12 million in FY16, primarily to support the increase in new business. However, net inventory was essential flat in the fourth quarter, reflecting improvement in materials management that we mentioned earlier. Accounts receivable declined $11 million in the fourth quarter, due to the timing of sales and our focus on reducing past-due accounts receivable.

Total debt was $842 million at September 30, reflecting repayments of $35 million in the fourth quarter, and $111 million in FY16. This brings the level of debt pay-down to more than $250 million over the past two fiscal years, and we expect to continue paying down debt into FY17.

In early October, we refinanced our term loan A and revolving credit facilities well-ahead of their maturity dates. The new facilities expire in 2021, with interest tied to the Company's leverage ratio. The new facility agreements also removed the interest coverage ratio requirement and extended the step-down provision of the leverage ratio requirement.

Please turn to slide 14. Cash from operations was $51 million in the FY16 fourth quarter, compared with $57 million in the same period last year. Free cash flow was $48 million, a conversion rate of more than 200% of net income. Free cash flow was $52 million in the fourth quarter of last year. Decreases in operating and free cash flow are primarily due to changes in working capital, primarily related to the timing of inventory receipts and sales related to account receivable. Now I will turn the call back over to Dave for closing remarks. Dave?

Dave Castagnola - *Wesco Aircraft Holdings Inc. - President & CEO*

Thanks, Rick. Please turn to slide 15. The scope and pace of transformational change is now largely behind Wesco. We delivered improved performance across the business, and better financial results compared to our recent history. As we enter FY17, momentum in contract sales is right on track. Our cost structure is more aligned with the sales opportunity for better leverage, profitability has improved, and our financial structure has been strengthened.

FY16 results provide the basis for a stronger FY17, based on new wins, scope expansion, and renewals secured during the year. The timing of sales from the new wins and expansion can be affected by a series of factors, as I noted earlier. The pace of implementation will influence the rate of growth during the year. We have considered these factors in our FY17 outlook. At the same time, we remain focused on margin improvement, supported by our material acquisition strategies, while considering the assumed timing of inventory turns for productivity realization.

In addition, we will remain focused on cost management. Cash management in FY17 will continue to be aligned with the expected improvement in inventory receipts and disbursements provided by our SIOP processes. This will enable us to continue our focus on reducing debt levels, and then begin to consider additional capital allocation strategies in FY18.

Please turn to slide 16. With these factors in mind, we are targeting in FY17 constant currency sales growth of 3% to 5%, adjusted diluted earnings per share in the range of $1.15 to $1.20, and free cash flow conversion in the range of 90% to 95% of net income. Again, it is important to point out that we based our sales outlook on business secured in FY16, and that our estimate is on a constant currency basis. Considering the time needed to implement new business and scope expansion, we expect greater sales increases in the second half of FY17. Also, we expect the first quarter of FY17 to be lower sequentially, due to fewer working days around the holidays, consistent with our experience in FY16.

Our adjusted diluted earnings per share range assumes that we improve gross margins through growth and cost efficiency, and that we manage our SG&A cost base. Our SG&A cost assumptions balance ongoing leverage with an improved cost structure, with investments to support new business, and incentives that reflect stronger performance in FY17.

Our outlook also reflects the higher effective tax rate that Rick mentioned earlier. Free cash flow is assumed to include inventory investment to support growth in the business, offset by efficiencies provided through working capital management. We also have provided a FY17 outlook on certain modeling items, which will you find on slide 17. I will now turn the call over the Jeff to direct the Q&A period. Jeff?

Jeff Misakian - *Wesco Aircraft Holdings Inc. - VP of IR*

Thank you, Dave. With that, we will open up the call to your questions. We ask that you limit your questions to one initially, to allow everyone a chance to participate, and we appreciate your assistance with this process. Anna, may we have the first question, please?

QUESTIONS AND ANSWERS

Operator

And we have a question from Jason Gursky from Citi.

Jason Gursky - *Citigroup - Analyst*

Good afternoon, everyone.

Dave Castagnola - *Wesco Aircraft Holdings Inc. - President & CEO*

Hi, Jason.

Jason Gursky - *Citigroup - Analyst*

I was wondering if we could dive a little bit more into the details on the revenue assumptions for 2017? And whether you could compare and contrast the expectations for North America versus Rest of World, and some of the assumptions that you have around ad hoc in your contract business? And maybe just provide a little bit of color on each of those items, would be helpful.

Dave Castagnola - *Wesco Aircraft Holdings Inc. - President & CEO*

Yes, I will provide an overview, and then have Rick give you the North America, Rest of the World view. So for ad hoc, we see ad hoc essentially flat going into 2017, and we've taken that into account in our planning, based on our experience of the market in 2016. We're not expecting any major disruptions or pinch points in the near term.

In terms of the contract business, that will be really the revenue momentum for 2017. And the pace of our implementations is really going to set the mid- to higher-end of our growth range, is the way we've guided. Rick, can you talk about, between the North America and the Rest of the World?

Rick Weller - *Wesco Aircraft Holdings Inc. - EVP & CFO*

Sure. Just to build on what Dave said, that the lion's share of the growth that we're seeing is business that we won in 2016, the larger strategic accounts. These are really our global customers. Some of them were referenced by Dave in his comments. They really are participating in largely our European arena, and North America. So I think our growth is pretty well-balanced between the regions, and also balanced across both hardware and chemicals, in terms of relative size and order of magnitude of that growth and where we think we would see it.

Jason Gursky - *Citigroup - Analyst*

Okay, that's great. And then really quickly on the cash conversion for next year decelerating from what you did this year, is there anything kind of one-off in nature that's going on next year that we should be aware of?

Rick Weller - *Wesco Aircraft Holdings Inc. - EVP & CFO*

Jason, the only thing I would say about that is that the nature of where our growth is emanating and coming from relative to strategic customer accounts requires us to be able to ramp up inventory to be able to support that. So you saw that both in the latter part of 2016, and you will see that into 2017.

Jason Gursky - *Citigroup - Analyst*

Okay, great. I will get back in the queue. Thanks, guys.

Dave Castagnola - *Wesco Aircraft Holdings Inc. - President & CEO*

Thanks, Jason.

Operator

Our next question is from Myles Walton from Deutsche Bank. Please go ahead.

Lou Raffetto - *Deutsche Bank - Analyst*

Good afternoon, good evening. This is Lou Raffetto on for Myles. Just quick question, maybe I missed it on the call earlier. The -- what you guys call that is the network rationalization -- what exactly is that? Any additional color on that one?

Dave Castagnola - *Wesco Aircraft Holdings Inc. - President & CEO*

Yes, hi, Myles, this is Dave. What we're referring to is, last year in the fourth quarter, we announced a major restructuring that talked about also part of our integration, the reduction of 13 to 16 sites. And what I was referring in to my comment is, we've completed that activity.

Part of it was based on our growth. We mentioned some investment that we made in Q4 for the growth. We've actually chosen to keep, I think, three open, because what happened was, we actually grew -- we won work in FY16 that really changed our mind, and we wanted to make sure that we retained our footprint there. So I was really referring to the action we took before and concluding that action.

Lou Raffetto - *Deutsche Bank - Analyst*

Okay, thank you.

Jeff Misakian - *Wesco Aircraft Holdings Inc. - VP of IR*

Thanks, Lou.

Operator

Our next question is from Gautam Khanna from Cowen and Company. Please go ahead.

Bill Ledley - *Cowen and Company - Analyst*

Hi, this is Bill Ledley on tonight for Gautam. Thanks for getting me in. Had a question for you on aftermarket sales. What were they as a percent of sales in FY16? And would do you think they will be in FY17?

And if you could just talk about pricing trends on the long-term contracts? Are they getting tougher? Are you seeing destocking from any of the OEMs? You called it out in the quarter. Do you guys assume that continues into FY17 at all?

Rick Weller - *Wesco Aircraft Holdings Inc. - EVP & CFO*

Yes, Bill, this is Rick. I will take the first one about the aftermarket. As we've kind of talked about, it is a focus area for growth for Wesco, but it's still a relatively small percentage at this point, of our total revenue, kind of 7% to 8% or so of the total revenue for Wesco. And I think over time, the size of the opportunity for growth and the focus we have on that will allow us to be able to continue to expand. But it will build off a relatively small base, and it is a relatively larger part of the served market in Wesco.

Dave Castagnola - *Wesco Aircraft Holdings Inc. - President & CEO*

And Bill, I will address the second question relative to pricing. I think, let me answer it a little bit broader. For a JIT LTA business, which is the long-term contract business we're talking about, that represents about 75% of our business, and that is an area of our business that is growing at the mid-single-digit pace that we talked about in 2016. And it's also the basis for what is leveraging our growth into 2017.

Our customers there really look at us on -- they evaluate us on a number of total-value propositions. We provide not only price -- because we can aggregate demand and provide them better pricing than they could get on their own -- but we also carry the inventory. In other words, we act as their inventory. We're on replenishment systems. So we improve their working capital and their cash management, which comes into play as they assess us. And in many cases, in particular with our chemical management system, we reduce scrap.

So with the working capital improvement, scrap reduction, the pricing that we can get from our partners, the better leverage for them, and then the fact that we manage that supply chain for them so they don't have to resource that SG&A -- all of those factors come into play from our customers when they're evaluating us. So it's not purely a price game.

On the ad hoc market side, it really depends on the urgency of the need. It depends on the number of the quotes that are going out. Price tends to come into play a little bit more on the ad hoc side. And again, we don't chase price relative to that market. So those are really the two areas of how we're evaluating going into the marketplace.

Bill Ledley - *Cowen and Company - Analyst*

Okay, that's great. And if I can just sneak in another one -- assumptions for SG&A as a percent of sales. This year it ticked down nicely, but that includes, of course, the FX. Any sense of where you think that goes next year?

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Rick Weller - *Wesco Aircraft Holdings Inc. - EVP & CFO*

Yes, Bill, going into 2017 -- obviously in 2016, we got a sizable benefit and a step-down function weight, with restructuring, and some of the benefits of site and supply consolidations, we've got some kind of continuing efficiency benefit going into 2017. But in relative terms, I think the contribution of SG&A leverage to the overall EBITDA margin leverage will be proportionally less.

And the other thing I would say is that the investments we're making in growth with facilities, site and supply, resources on the ground or direct labor, and even funding incentive plans, the anticipation of a good year. Those things are going to make the SG&A have a little bit of lift, that we use the efficiency I just mentioned to lift off that.

Bill Ledley - *Cowen and Company - Analyst*

Okay, great. Thank you very much.

Rick Weller - *Wesco Aircraft Holdings Inc. - EVP & CFO*

You're welcome.

Operator

(Operator Instructions)

Sheila Kahyaoglu from Jefferies. Please go ahead.

Sheila Kahyaoglu - *Jefferies & Company - Analyst*

Hi, good afternoon. Thanks for taking my question.

Jeff Misakian - *Wesco Aircraft Holdings Inc. - VP of IR*

Hi, Sheila.

Sheila Kahyaoglu - *Jefferies & Company - Analyst*

Hi. I guess, is there a metric that you could talk about, whether it's your order book or your backlog, or however you think it's best to measure it, the difference in visibility today as you look out to 2017 versus a year ago? If could you talk about maybe -- I don't know what metric you would look at?

Dave Castagnola - *Wesco Aircraft Holdings Inc. - President & CEO*

Yes, hi, Sheila. This is Dave. Well, a couple of things. I think we don't really talk about the total value of renewals or the longer-term backlog, and we haven't really talked about the total values of our win. You can see that the latter is the secured wins that will fuel our growth next year into FY17.

If you contrast FY16 with FY17, it's really about the momentum in the business. As I mentioned in my comments, coming into FY16, Wesco was coming off a significant sales decline in 2015, with little to no momentum in contract sales wins, and had some ad hoc momentum in the final four months of that year. So we looked at, coming into this year, to bridge the ad hoc sales while we recovered on the contract side.

And what played out is, we recovered quite well, and now have gained significant momentum on the contract side, which is the basis of our business. So the big difference going into this year versus last year is that our plan is really based on secured JIT LTA-type business, which is the bulk of what we do.

Sheila Kahyaoglu - *Jefferies & Company - Analyst*

Okay. And then you mentioned some second-half weighting, and the timing of implementation. Is that just when the supplier might place an order? Or can you clarify what the implementation really means?

Dave Castagnola - *Wesco Aircraft Holdings Inc. - President & CEO*

Yes, it's all those things. And so let me start at a macro level, and then work my way down. At a macro level, I think the chemical management implementations go a little bit faster and are a little bit less complex than hardware implementations.

Hardware implementations have a lot of factors. You mentioned a couple, and I mentioned in my comments, whether it's -- if it's a brand-new market and brand-new products, there's lead time involved. If it's a customer that we are expanding market share into, sometimes we have to work through depletion of their inventory as we bring ours in line. And others where we already have a position and we are growing, we can leverage that inventory and demand.

So there's a lot of different factors involved in the front end. So that's why we've resourced an implementation team, and we are managing by implementation, by site, by customer, each one of these unique implementations, to ensure that we hit all the milestones accordingly.

Sheila Kahyaoglu - *Jefferies & Company - Analyst*

All right, that's very helpful. And then last question, if I could sneak it in -- in terms of Q4 in international, Rest of World sales, organic sales were up significantly. Can you point to maybe one or two customers that are driving some of that strength?

Rick Weller - *Wesco Aircraft Holdings Inc. - EVP & CFO*

It was really multiple customers. Obviously big OEMs and Tier manufacturers in Europe, and it was really across both chemicals and hardware. So the good thing is, it was very balanced and a very focused effort. The other thing I would mention too, is that, unlike North America, they actually got quite a bit of help from ad hoc. So there was quite a bit of transference and quite a bit of ad-hoc buying activity in Europe that was markedly different than what we saw in North America. So both of those really drove the growth.

Sheila Kahyaoglu - *Jefferies & Company - Analyst*

Great. Thank you very much.

Rick Weller - *Wesco Aircraft Holdings Inc. - EVP & CFO*

You're welcome.

Operator

And we have another question from Gautam Khanna from Cowen and Company.

Bill Ledley - *Cowen and Company - Analyst*

Thanks, guys. Just had one quick follow-up. In regards to the destocking comment in Q4, can you perhaps size or maybe talk about the potential risk to the revenue guidance if Boeing takes down their rates on the 777?

Dave Castagnola - *Wesco Aircraft Holdings Inc. - President & CEO*

So yes, I think what we -- and my comment there was really, manufacturers have been talking about OEM inventory adjustments, and we've seen other -- and mentioned other distributors destocking. We certainly haven't. We are not seeing any really demand reduction associated with the rates, associated with the wide-bodies.

Again, if those -- those are happening to our customers because of our position and balance with our customers, and also with our market, 40% military, 60% commercial. We're real balanced in. And as I've said in a number of earnings calls, when we provide our product in, it goes on essentially all platforms with our customers. So we have a real good buffer against their perturbations. In other words, if they have a sun-setting program on decline, and they have a ramping-up production program and a start-up program, we balance out.

That said, because of the nature of our business, we feel their production lines real-time, because we're on an MRS replenishment system. So unlike a large tier 1, where we have constant large -- or LRU product deliveries, we're on a daily cadence basis. So we get a bit of oscillation, but over time, it's relatively simple, and we buffer out big swings relative to unique platforms in the market.

Rick Weller - *Wesco Aircraft Holdings Inc. - EVP & CFO*

Maybe I would add one other point to that, which is that build rates really don't influence chemical consumption or chemical management service the same way it does hardware. So that's just another element to build on what Dave is saying of kind of diversification and reliance on specific platform build rates.

Dave Castagnola - *Wesco Aircraft Holdings Inc. - President & CEO*

I think the final point on that really is what we're experiencing here in 2016, going into 2017, is some significant momentum with new wins and scope expansion. So if there is any perturbations in a particular segment of the market, we're growing through that with our customers by adding new product lines, expanding scope and/or winning new business.

Bill Ledley - *Cowen and Company - Analyst*

That's great. If I could just follow up on the chemical sales point, embedded within the guidance of 3% to 5% is -- are chemicals still outpacing the growth of hardware?

Rick Weller - *Wesco Aircraft Holdings Inc. - EVP & CFO*

They're pretty well-balanced into 2017. So a lot of our strategic account wins are coming as a result of scope expansion, taking on new sites, and cross-selling chemicals into hardware sites, and vice versa. So it really is pretty balanced.

Bill Ledley - *Cowen and Company - Analyst*

All right, great. Thank so you much, guys. Good luck.

Dave Castagnola - *Wesco Aircraft Holdings Inc. - President & CEO*

Thank you, Bill.

Operator

And we have a question from Myles Walton with Deutsche Bank. Please go ahead.

Lou Raffetto - *Deutsche Bank - Analyst*

Hey, guys. Just wanted to follow up on the EBITDA margin expansion. I know it was up 50 bps, and you said 30 bps of headwind from FX, and then I think a little bit more from investments. What are you thinking about for 2017?

Rick Weller - *Wesco Aircraft Holdings Inc. - EVP & CFO*

Yes, Myles, I think going into 2017, it's going to really line up pretty well with the EPS guidance. So same kind of relative range of earnings, because, based on the share count, you've got the -- a little bit of pull based on the tax rate. But that would kind of give an indication of what EBITDA margin expansion would be just as a function of what we're guiding in terms of earnings per share.

Lou Raffetto - *Deutsche Bank - Analyst*

Okay, thanks, guys.

Rick Weller - *Wesco Aircraft Holdings Inc. - EVP & CFO*

Sure.

Operator

And we have a question from Jason Gursky from Citi. Please go ahead.

Jason Gursky - *Citigroup - Analyst*

Hey, guys. Just a quick follow-up, and maybe try to wrap up and bring together a couple of prior questions. One was about visibility and how far out you guys feel you can see with your customers, and the 777 question. We know the 777 rates are coming down next year. And it looks like there could be further pressure on that rate as we move out into the fourth quarter of 2017 and into 2018.

So the question is, have you already -- do you feel like what's in your guidance today already reflects the decline that we're going see in the 777 here in 2017? Because you suggested that you're getting your revenues in real-time from your customers. I'm just wondering, what kind of build plan, and how far out are they showing you their needs as we move here into calendar 2017? I just want to confirm that 777 is fully baked here, because it is coming down.

Dave Castagnola - *Wesco Aircraft Holdings Inc. - President & CEO*

Yes, thanks, Jason. Yes, we've taken that -- we take that into account with all our customers. We get visibility from them as far out as they have from their customers, and they provide it to us. We've gotten much more rigorous in our ability to plan here at Wesco.

We've got basically customer by customer, program by program, and we can look at where we've got momentum, where there is momentum growth, where there's momentum decline. And we've done our best to plan it into FY17, and taken that into account. And then from that, we have layered in the new business wins.

So we've been, we believe, very thoughtful about that. And then we've also, again, based on the leverage for growth, been very thoughtful about how we've taken into account the timing of the implementations to get that done. So we think we've got everything we know planned for.

Jason Gursky - *Citigroup - Analyst*

Okay. Were there any 10% customers, either in the quarter or for the year, for you guys?

Rick Weller - *Wesco Aircraft Holdings Inc. - EVP & CFO*

No.

Dave Castagnola - *Wesco Aircraft Holdings Inc. - President & CEO*

We don't have anybody that big.

Jason Gursky - *Citigroup - Analyst*

Right, okay. And then the last one here would be just maybe a few comments about what you view to be the biggest risks and the biggest opportunities for 2017? If we were to come to the end of the year and you beat your guidance, why did it happen? And if you were to miss it, why do you think it might have happened?

Dave Castagnola - *Wesco Aircraft Holdings Inc. - President & CEO*

Yes, I think on the opportunity side, it's just really about the execution and pace of the implementations. So obviously Wesco has never had this level of sales success and this volume of new product implementation. So we're excited about that. And how well that comes in as we've predicted -- there's a lot of variables involved. So I would like to get a few quarters under our belt without seeing that materialize, and I'll feel really good about that.

I think the only risks associated with the business are just macro risks that the whole market has, and we would react accordingly to those. I think one of the benefits Wesco has that I see is that our model, our service actually provides a reduction of costs. So there's an opportunity to be opportunistic if, in fact, there was a macro event in the market, where some of our customers would be looking to reduce costs, we can pull on a lot of that.

So if you contrast this year to last year, last year was really depending on the ad hoc market developing and growing, and the ad hoc market ended up being soft for the reasons we talked about. This year we have the work, it's secured. And it's just really about how well we've timed it and planned that implementation.

Jason Gursky - *Citigroup - Analyst*

That's great. Thanks, guys.

Operator

And we have no further questions at this time. I would like to turn the call over to Jeff Misakian for closing remarks.

Jeff Misakian - *Wesco Aircraft Holdings Inc. - VP of IR*

Okay, great, thanks, Anna. On behalf of everyone at Wesco Aircraft, I would like to thank you for your participation today. We appreciate your interest in Wesco, and look forward to speaking with you all again really soon. Thanks, and have a great evening.

Operator

Thank you, ladies and gentlemen. This concludes today's conference. Thank you for participating. You may now disconnect.
