LIHUA INTERNATIONAL
LIHUA INTERNATIONAL FIRST QUARTER 2011 FINANCIAL RESULTS
Transcript

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Chairperson: Lee Roth (Mgmt.)

Operator: Good morning ladies and gentlemen. Thank you for standing by. Welcome to the Lihua International First Quarter 2011 Earnings conference call. During today's presentation, all parties will be in a listen-only mode. Following the presentation the conference will be open to questions. If you have a question please press the star followed by the one on your touchtone phone. Please press star, zero for operator assistance at any time. If you are using speaker equipment, it may be necessary to pick up your handset before making a selection. This conference is being recorded today, Tuesday, May 10, 2011.

I would now like to turn the conference over to our host, Mr. Lee Roth of the Piacente Group. Please go ahead.

Lee Roth: Thank you, Luke, and good day everyone. This is Lee Roth with the Piacente Group, investor relations counsel for Lihua International. Joining me from management are Chairman and Chief Executive Officer, Mr. Jianhua Zhu; Chief Financial Officer, Mr. Roy Yu; and EVP of Corporate Finance and Director of Investor Relations, Ms. Daphne Huang.

Before we begin, I'd like to remind you that the comments made during today's call may contain forward-looking statements within the meaning of Section 27(a) of the Securities Act of 1933, as amended, and Section 21(e) of the Securities Exchange Act of 1934, as amended. All statements other than statements of historical fact that address activities, events or developments that the Company expects, projects, believes or anticipates will or may occur in the future, including but without limitation to statements about Lihua's business or growth strategy, general industry conditions, including the availability of copper or recycled scrap copper, future operating results of the Company, capital expenditures, expansion and growth opportunities, bank borrowings, financing activities and other such matters are forward-looking statements. Although the Company believes that its expectations made during today's call and during the related Q&A session are based on reasonable assumptions, our actual results may differ from those projected in the forward-looking statements.

With that said, it's now my pleasure to turn the call over to Lihua's Chairman and Chief Executive Officer, Mr. Jianhua Zhu. Mr. Zhu, go ahead please.

Jianhua Zhu: [Chinese spoken]

Daphne Huang: Thank you, Mr. Zhu, and good morning everyone, and thank you all for joining us today via telephone and over the Internet. I would like to start today's call by providing some translated comments from Mr. Zhu, our Chairman and CEO. We began 2011 with continued robust growth across our key operating metrics, including a new quarterly sales record of 136.9 million, representing 117% increase over first quarter last year. Our top and bottom line growth came from continued strong demand from both our CCA and copper wire and copper anode products, as well as our timely increase in refinery capacity during the third quarter of last year.

On a non-GAAP basis, which excludes charges related to the change in fair value of warrants and gain on extinguishment of warrant liabilities, our quarterly net income was up 50% over last year to 11.1 million or $0.37 per diluted EPS. First quarter EBITDA increased by 47% compared with last year to 15.7 million or $0.52 adjusted diluted EPS.

Turning to our sales, the performance of copper anode since its launch in July 2010, demonstrates our ability to anticipate and address emerging trends in the markets. In the first quarter, revenue from copper anode reached 66 million or roughly 48.2% of our total quarterly sales, despite some seasonal weaknesses related to the Chinese New Year in February. Again, I would like to point out, though, that as copper anode increases as a percentage of revenues, it will impact our gross margin percentage as the product carries a lower margin than our wire products. Despite the lower margins, our refined copper products carry a number of distinct advantages compared to higher margin wire products. Copper anode is characterized by a much shorter production cycle than wire, allowing us to benefit from increased cash conversion and a greater return on invested capital.

As we've noted in the past, it takes roughly seven days to turn one ton of scrap copper into a ton of copper anode or copper rod, whereas turning that same ton of scrap into a ton of copper wire takes approximately 30 days. This significantly shorter production cycle allows us to produce much higher volume of copper anode than wire over a given period of time, resulting in increased revenue generation and extended profitability in absolute dollars.

In the first quarter, our overall gross margin decreased to 12.3% compared with 18.7% in the same period last year and 15.2% in the fourth quarter of 2010. While our margins will likely trend down as a result of the continued shift towards copper anode, we expect to see continued solid performance on the revenue line and gross profit dollars, based on the points I just mentioned of increased volumes and return on invested capital, ultimately contributing to greater overall profitability.

Since launching copper anode, demand has been well above what we have been able to produce. We've been running at 100% capacity with additional orders and product inquiries coming in regularly. Construction at our new plant and copper recycling facility is proceeding according to plan and we are on track to launch production on the two new smelters, doubling our annualized capacity on the smelting side to 100,000 tons by the start of the fourth quarter. We plan to allocate a total of 75,000 tons of smelting capacity to copper anode with the remaining 25,000 tons allocated to copper rod, the majority of which will be consumed internally as a raw material for superfine copper wire.

We're currently evaluating additional capacity expansion opportunities following the launch of our new facility. It is important to point out that although this construction project is expected to take roughly nine or ten months, incremental capacity additions will be much less time intensive with the construction of a new smelter in an existing plant expected to take three to four months on average. To the extent that we would like to increase wire production capacity as well, the construction and installation of a new wire drawing line would also take between three and four months.

In addition to our ongoing capacity expansion efforts, we remain committed to further innovation in the development of new and value-added products and reducing the environmental impact of our manufacturing processes to extend our leadership position in the development of new copper recycling technologies. The Chinese government is imposing tighter environmental regulations on manufacturing companies in an effort to reduce energy consumption and carbon emissions. We are proud to say that our current recycling technology meets or exceeds all environmental standards, while producing a product that achieves a level of purity other recyclers cannot match at prices that are lower than mined copper and comparable to other refined copper products.

I'm pleased to say that our commitment to environment excellence in additional to operational success has resulted in several recent distinctions for Lihua. First, we recently formed a partnership with one of China's top research institutes, Beijing Modern Research Institute of Recycling Economy, also known as RIORE, through which we will establish a new joint R&D center at our headquarters in Danyang which will focus on the study of copper recycling with the goal of developing new environmentally-friendly products. RIORE is one of China's foremost environmentally focused research institutes and we are very excited about the possibility that this collaboration presents for our company, for our partnership, and for the industry as a whole.

Also of note, earlier this month our two subsidiaries received ISO 14001:2004 certification for environmental management systems by the International Organization for Standardization. This certification relates to our CC and copper wire, copper anode and copper rod products and the associated production processes, and includes rigorous assessments of management systems, operations and environmental systems. We are proud that the ISO has recognized our commitment to environmental responsibility and we will continue working to ensure that our operation adheres to the highest possible environmental standards, while our products adhere to the highest possible standards of quality.

In addition to our recent environmental accomplishments, our Company was also recognized by the Danyang government for operational excellence, innovation and internal controls. Being recognized by our government as a key contributor to the city's economic growth, a leading innovator in China's copper industry, and a top corporate citizen in the region was a tremendous honor for Lihua. These awards lend credibility to the significant efforts throughout our organization to drive growth, technological innovation, and continuous improvements in our internal controls and processes, and motivate us to reach even greater heights.

As we've stated in the past, we do not believe that our performance and outlook are accurately reflected in the price of our shares. As a result, we received approval from the Board of Directors in January to repurchase up to 15 million of the Company's common shares over the next 12 months. Through March 31, 2011, we have purchased approximately 97,600 shares at an average price of $9.49 through open market transactions. We are committed to execute on our repurchase program and will update our progress on a quarterly basis.

Based on current market trends and the assumption that we will launch production at our new recycling facility at the beginning of the fourth quarter, we are affirming our 2011 guidance of gross profit, ranging from 80 to 82 million and non-GAAP net income ranging of 52 to 54 million, which represents year-over-year growth of 29 to 32% and 30 to 35% respectively. As mentioned, these projections assume one quarter of copper anode sales contribution from our two new smelters currently under construction. They also do not factor in any potential benefit from our import license, which will improve gross profit due to the ability to directly purchase raw copper from suppliers abroad.

Overall, the first quarter in 2011 has gotten off to an excellent start for Lihua both operationally and strategically. Our growth outlook remains strong and we see great opportunities ahead of us for 2011 with our end markets continuing to grow at a very healthy pace, construction at our new copper recycling facility progressing, and approval for our import license expected in a matter of a month or two. We have a number of significant talents that will help to drive Lihua's continued operational and financial success.

Our business is strong and growing, thanks to our best-of-breed products and stellar reputation in the markets we serve. We have a clear and achievable growth strategy that is built around significant capacity expansion, improving raw material sourcing capabilities, and introducing new value-added products to create additional market opportunities for Lihua. We are excited about what the future holds for Lihua and look forward to sharing our progress and successes with you as we continue to move forward.

With that overview, I would now like to turn the call over to our CFO, Roy Yu, to review our financial results for the quarter. Roy?

Roy Yu: Thank you, Mr. Zhu, and thank you, Daphne. Before I provide an overview of our financial results, I'd like to highlight that all of our financials are prepared in accordance with U.S. GAAP. In addition to GAAP reporting, we will be providing EBITDA and non-GAAP net income, which are non-GAAP measurements. We believe that EBITDA and non-GAAP net income are important metrics that provide investors with information about our operating trends. We define non-GAAP net income as net income excluding the changes in fair value of warrants and other one-time or non-recurring items that are evaluated on an individual basis. We define EBITDA as net income before discontinued operations, interest expense, income tax, depreciation and amortization, net operating income expense, and non-cash share-based compensation expenses.

With that said, our sales for the first quarter of 2011 increased 117% to $136.9 million compared with sales of $63.2 million in the first quarter of 2010. The increase in sales came from both CCA and copper wire products as well as copper anode, which generated sales of $70.9 million and $66 million respectively in the first quarter of 2011.

Our revenue and volume breakdown on a sequential quarter basis for each product was as follows: the first quarter, we sold 6,724 tons of CCA and copper wire for $70.9 million in sales, compared with 8,049 tons for $73.5 million in sales in the fourth quarter of 2010. Copper anode volume in the first quarter totaled 6,996 tons accounting for $66 million of revenue, compared with 7,464 tons or $61.9 million of revenue in the fourth quarter of 2010.

On a year-over-year comparative basis, in the first quarter of 2010 we sold 4,678 tons of CCA and copper wire for revenue of $40.6 million, and 2,997 tons of copper rod totaling $22.6 million. There was no copper anode sold as the product was not introduced until the third quarter of 2010.

Our gross profit by product for the quarter was as follows: copper and CCA wire product accounted for $11 million of gross profit or $1,632 per ton compared with $15 million or $1,864 per ton in the fourth quarter of 2010. Copper anode contributed a total of 5.9 million to gross profit or $848 per ton compared with $5.6 million of gross profit or $751 per ton for the last quarter. For the first quarter of 2011, our gross profit increased 43% to $16.9 million or 12.3% of sales. This compares with gross profit of 11.8 million or 18.7% of sales for the first quarter of 2010. The decrease in gross margin as a percentage of sales is principally due to continued shift in product mix to refined copper products, which carry lower gross profit margins than Lihua's wire products but have a much higher return on invested capital due to a significantly reduced production cycle and higher volume output.

Selling, general and administrative expenses for the first quarter of 2011 were $2.1 million compared with $1.7 million in the same period in 2010. The increase in SG&A was primarily due to increased costs related to production, distribution and insurance as a result of expanded business, as well as higher administrative and professional fees associated with the Company being a public reporting company and our extended scale of operations.

For the three months ended March 31, 2011, our income tax expense was $3.9 million reflecting an effective tax rate of 23.9% from operations. This compares with income tax expense of $2.7 million and effective tax rate of 23.4% for the three months ended March 31, 2010.

For the first quarter of 2011, our other comprehensive income included foreign currency translation adjustment gains of $1.7 million. This compares to a gain of approximately $48,000 in the same period last year. Net income for the first quarter of 2011 was 12.5 million or $0.41 per share, based on 30.3 million weighted average diluted shares outstanding. This compares with net income of $8.9 million or $0.34 per share, based on 26.3 million weighted average diluted shares outstanding in the first quarter of 2010.

Non-GAAP net income for the first quarter of 2011 was 11.1 million. This compares with non-GAAP net income of 7.4 million for the first quarter of 2010. Non-GAAP net income excluded gains related to the change in fair value of warrants and the extinguishment of warrants liability totaling approximately $1.4 million and $1.5 million for the first quarter of 2011 and 2010 respectively.

EBITDA for the three months ended March 31, 2011 was $15.7 million, a 47% increase compared with EBITDA of $10.7 million for the same period in the prior year.

Turning to the balance sheet, we finished the quarter ended March 31, 2011 with $90.7 million or $2.99 per diluted shares in cash and cash equivalents compared with 90.6 million as of December 31, 2010. As Daphne mentioned, for the 2011 guidance Lihua is affirming 2011 gross profit of $80 million to $82 million and non-GAAP net income of $52 million to $54 million, representing year-over-year growth of 29 to 32% and 30 to 35% respectively. We expect 2011 growth will be driven by the introduction of Lihua copper's recycling facility in the second half of 2011 with continued strong demand in China for recycled copper and copper alternatives in the household appliance, consumer-wide goods and infrastructure markets. The new copper recycling facility will initially house two new 25,000 ton smelters. Additional space in the new plant will allow us to continue organic growth in the near future.

To summarize, the first quarter kicked off what we believe will be a great year for Lihua. We achieved significant growth and are well-positioned to benefit from increased capacity, improved procurement from our pending import license, as well as our enhanced R&D capability through the RIORE collaboration. We are excited about what the future holds for our company for the remainder of 2011 and well into the future. On behalf of Mr. Zhu and the rest of our management team, we hope you share that excitement.

Our business is growing and we have solid operations in which we are strategically expanding our capacity to further our growth. Our doors and phones are open to investors and we welcome you to come visit our facility to help those that are interested truly understand our business operations. We also invite you to join us in Danyang for our first ever investor analyst day on May 24th so that you can see our operations firsthand. In addition, I'd like to add that we are on schedule to file our 2010 SAIC report in June. We will be posting this report to our website along with reconciliation to our 10-K filing. As a reminder, our 2009 SAIC filing and reconciliation is also available on our website. Transparency is of the utmost importance to us and we invite you to review these filings and reconciliations firsthand.

With that said, I would now like to open the lines to your questions. Thank you.

Operator: Thank you, sir. We will now begin the question and answer session. As a reminder, if you have a question please press the star followed by the one on your touchtone phone. If you would like to withdraw your question, please press star followed by the two. If you are using speaker equipment, we will need you to lift the handset before making your selection.

Your first question for today comes from the line of Dmitriy Shapiro with Global Hunter Securities. Please go ahead.

Dmitriy Shapiro: Hi guys. Congratulations on the quarter.

Roy Yu: Thank you, Dmitriy.

Dmitriy Shapiro: My first question is regarding your share repurchase plan. Is it current with plans and will the Company be able to commence the share repurchase as soon as it exits the blackout period?

Roy Yu: Dmitriy, sure. You know, we are 100% committed to the stock buyback repurchase program, and also I think you will see the action once we get out the blackout period.

Dmitriy Shapiro: Okay, great. And also, assuming you're able to repurchase the full 15 million at reasonable prices, would you consider increasing the share repurchase after Q2 if share price were to remain near current levels?

Roy Yu: Yes. That's actually what we discussed with our Board in our first Board meeting this year, and we have got support from our Board of Directors.

Dmitriy Shapiro: Okay, excellent. Sounds great. There has been a number of articles recently discussing the overcapacity in China's copper supplies, which could lead to a drop in copper prices and potential slowdown in demand. Do you expect this to affect the demand for your products, your sell-through, or your profitability?

Daphne Huang: We'll ask Mr. Zhu to answer this question. Hold on a second. Let me translate for him. (Chinese spoken)

Jianhua Zhu: [Chinese spoken]

Daphne Huang: Great, okay. Mr. Zhu basically commented that the copper price fluctuation in China follows the trend of the worldwide copper price fluctuation; however, in terms of the product and the business that we are selling and we're in, which basically we essentially employ scrap copper as raw material for our high quality refined copper products, we don't see any slowdown in demand. That really—this trend is really due to the macro situation of the domestic continued infrastructure build-out, the continued domestic demand in the end products that we're selling to in terms of markets, and we're very confident that we're going to see a very good future in terms of growth in all the products that we're selling.

Dmitriy Shapiro: Okay, got it. Great. I'm also a bit confused by the cash flows for the quarter. I was expecting DSOs to decrease and cash flows to be much stronger for Q1 as the anode business ramps, but it looks like DSOs actually increased by a day or two. Can you better explain what is going on there?

Roy Yu: Right, Dmitriy. So as you can see, we increased the capacity so during the first quarter, remember in our business model as we receive the customer order first and, you know, once after that we're going to book the raw material. So during the first quarter after the Chinese New Year, we received big orders from our customer. So once we have the order, we have to secure more raw material, which is the inventory. So as you can see in the cash flow—sorry, hold on for a second, Dmitriy. Yes, so the inventory actually increased $6.7 million. I think that's the biggest impact to the operating cash activity and the cash flow.

Dmitriy Shapiro: Okay, right. Got it. So my final question, many analysts and investors have been suggesting that you guys upgrade to a tier one auditor. Can you tell us if this is something that you're currently pursuing and where you are with the process?

Roy Yu: We will do the best to maximize our shareholders' value. If that's necessary, we will do it definitely to upgrade to one of the big four.

Dmitriy Shapiro: Okay, thank you. I'll jump back into the queue.

Roy Yu: Thanks, Dmitriy.

Jianhua Zhu: Thank you.

Operator: Your next question comes from the line of Katya Voronchuk of Rodman & Renshaw. Please go ahead.

Katya Voronchuk: Good morning, guys. My first question is actually a follow-up question on the demand. Can you please give us an update on the current spread between refined copper and scrap copper prices, and the impact that this price may have on the demand for your products and also mark-ups on your products?

Roy Yu: Yes. Currently, the new copper price is about 60—it's around 69,000 RMB per ton, and scrap copper is about 59.

Katya Voronchuk: Is that including VAT or excluding VAT?

Roy Yu: Including VAT.

Katya Voronchuk: Okay.

Roy Yu: Yes. So the difference is about $9,000 as the new copper price dropped recently, and we believe the scrap copper will follow the trends, going to decrease slightly in the near future.

Katya Voronchuk: Okay. And can you just kind of talk a little bit on how does this spread affect the shift in demand between refined copper and scrap copper, because my understanding is that if this spread falls below a certain level, some of the purchases will switch to buying refined copper.

Roy Yu: I'm sorry, Katya. Can you repeat your question? I didn't get it.

Katya Voronchuk: Sure. Basically, the question is if this spread between refined copper and scrap copper falls below a certain level, some of the companies that purchase copper may switch to buying refined copper instead of buying recycled copper.

Roy Yu: Okay, I got it.

Katya Voronchuk: Do you think that this 9,000 RMB number, do you think it's going to help the demand for your products or do you think it may actually shift the demand towards refined copper?

Roy Yu: I think this is—you know, going back to the historical price, I mean, the price difference between the virgin copper and scrap copper. 9,000 RMB is a normal range. It's normally between 8,000 to 12,000 RMB per ton. Well, it's still going to be—it's still going to be cheaper for using scrap copper versus virgin copper, and another point I want to make here—you know, most of our customers, they don't care about what copper we're using. So, they only care about the conductivity and resistance of our products. And you know, because we can provide high quality copper from recycled copper, we can see very strong demand in the market for Lihua products.

Katya Voronchuk: I see. And—

Daphne Huang: Katya, when you say refined copper, do you mean from really the copper products from the virgin copper powder, from the copper mines?

Katya Voronchuk: Correct.

Daphne Huang: Okay. Well we haven't seen—it's been interesting, but historically over the past many years we really haven't seen the reverse in the pricing trend between the scrap copper and the virgin copper price. So obviously there is reasonable belief on the Company's part that this trend is going to continue. Should for a doomsday scenario that in China right now, the copper is still a very high value commodity in China right now, because of the shortage domestically in copper resource, but let's say should the virgin copper supply in China for whatever reason is in an oversupply situation, and the price dips temporarily below the scrap copper price, I think most likely we can almost be certain that will be a very temporary phenomenon. So long term overall, it's not going to—or even in a matter of more than a couple months, it's not going to impact our total profitability of the business.

Katya Voronchuk: Okay, thank you. And another question—considering that you're running at 100% capacity, can you comment on your capacity expansion plans beyond the two smelters that you're currently building?

Roy Yu: I believe it's—you know, we—we're going to keep increasing the smelting capacity, as well as we also have a plan to increase the drawing capacity. But, you know, currently we're still in R&D for new products so there is no formal decision made by the Company yet.

Katya Voronchuk: Okay. Okay, that's—

Daphne Huang: But it's still—sorry. Just to follow up on Roy's point, one thing that everybody needs to keep in mind is once the basic infrastructure of the plant is built, in terms of whether adding a new smelter or adding a new drawing line, production line, it's really maximum three to four months of construction and installation before ramping up. So management does have the flexibility in terms of timing to really consider in the near term capacity expansion toward which direction.

Katya Voronchuk: Okay, thank you; and again, congratulations for the great quarter.

Daphne Huang: Thanks.

Roy Yu: Thanks.

Operator: Your next question comes from the line of Jay Srivatsa of Chardan Capital Markets. Please go ahead.

Jay Srivatsa: Yes, thanks for taking my questions and congratulations on a good quarter. You made a comment about you're expecting the importers license to have a positive impact on your current gross profit and net income. Could you try to quantify for us what type of impact you expect, and when do you expect the license to come to materialize for you?

Roy Yu: Yes, Jay. Based on the information we currently have, Lihua's passed all the passing by the government and we should receive our import license by the end of May, in another two or three weeks.

Jay Srivatsa: Okay. And what type of impact do you expect that would have on your gross profit line?

Roy Yu: I believe based on our current calculations, I believe it would be at 150—around $150 per ton to gross profit. And I think one thing I want to point out here is the importance of the import license is not only for giving us more gross profit per ton basis. And as you know, it's always very difficult for a company in China to get money offshore, but getting this import license, we can—the Company is going to have the flexibility to leave the profit in our Hong Kong subsidiary, so that means we can have a lot of cash offshore in the future, which we can use that cash for dividend or increase the share repurchase program.

Jay Srivatsa: Sure. So this $150 per ton increment to gross profit is currently not in your guidance, is that right?

Roy Yu: No, we didn't put that into our guidance because currently we are talking to the—our four biggest scrap copper suppliers in the U.S., so we have passed the due diligence from these big suppliers. So once we have that import license, we're going to do some trial orders with these suppliers, and then I believe should we start from—in the fourth quarter, we should be—start to import big volume from overseas.

Jay Srivatsa: Thank you very much.

Roy Yu: Thanks, Jay.

Operator: Ladies and gentlemen, if there are any additional questions, please press the star followed by the one at this time. As a reminder, if you're using speaker equipment, you'll need to lift the handset before making your selection. One moment, please, for your next question.

Your next question comes from the line of Steve Tabb of Tocqueville. Please go ahead.

Steve Tabb: Hi. I'm wondering—you're greatly increasing your sales of rods from smelting. How much of it is going into just a couple of your largest customers, and how high will your receivables go from the two customers, as a result of your increased production? How big a concentration, in other words, are you going to have in the receivables of these two large customers?

Roy Yu: Currently, our largest customer is on copper anode side. Remember, we signed a long-term contract with one of the biggest copper companies in China, but for that type of product normally we get paid at delivery after we passed the testing. So 70% of the money will be paid to us and the rest of the 30% will be paid to us within 30 days after the delivery. So we—given that kind of—type of payment terms, we shouldn't have too much concentration on one customer.

Steve Tabb: Yes, but I'd still like to know. You've doubled it and you're increasing it again. I'd like to know how much, in other words, of the receivables—what percentage of your total receivables are going to come approximately from these two big customers?

Roy Yu: Hold on a second. Let me—let me double check the number for you. I believe it's around 10%.

Steve Tabb: Okay. Now, would you remind me when do the warrants expire that you have outstanding?

Roy Yu: The warrants?

Steve Tabb: Yes.

Roy Yu: Okay. So we called up our Series A warrants in the first quarter. So currently, we have about 460,000 warrants outstanding.

Steve Tabb: And when do they expire?

Roy Yu: Five years from the issuance.

Daphne Huang: The Series B warrants were issued back in September of 2009, so there will be a few more years.

Steve Tabb: I see. And how many did you call up, did you say?

Roy Yu: Yes, the Series A we had was 1.5 million. We issued in 2008, October, when we did the Private Placement transaction.

Steve Tabb: So you called—you reduced it by a million warrants during the quarter, is that what you're saying?

Roy Yu: No, we called—it's about 600,000 Series A left during—in the—when we called the Series A.

Steve Tabb: Mm-hmm, I see. So you called 600. Thank you. Now—600,000 warrants. Can you—when does your quiet period end now, so that you can start repurchasing?

Roy Yu: That's three days after we file the 10-Q—three business days after we file the 10-Q.

Steve Tabb: You're filing it very soon, now, aren't you?

Roy Yu: Yes, we file today.

Steve Tabb: File today. Okay. Now, why—what is the math—I mean, I see your gross profit—we see your gross profit goes down drastically as a percent by just doing smelting. But you seem to have a very good gross profit on the—drawing the wire, and you have plenty of cash. I don't understand why you don't make a further effort to increase the drawing capacity on an accelerated basis.

Roy Yu: The reason—okay. So the reason we make this decision is because for the drawing profit, it takes much longer time. On average, it's about 30 to 45 days, depends on the diameter of the wire we produce. So that will require a larger working capital. So currently, as you can see, we have $90 million cash in hand, but that's not only capital. It's also working capital. Remember what I just mentioned at the beginning of the month, we always receive big orders from customers, and at that time we need cash to secure our raw material. So with that $90 million, I think we can spend a lot of cash within there to buy raw material. And at the end of the month, after we deliver all the products to our customers, we're going to collect the money back. So you can see the cash is not only the capital, it's also working capital. But given the cycles for the production of wires, we're going to need much more cash for adding more capacity, given the current copper price. And also, if you do some calculations on the return on invested capital, you can see because copper anode taking much shorter time until the invested capital could be better than wire products.

Steve Tabb: I still don't—I mean, it's hard for me to understand. I mean, the difference in the gross profit is, what, about 10% or more?

Roy Yu: On anode?

Steve Tabb: Yes, from anode to drawing wire.

Roy Yu: The average—on average, yes. Anode has the lower gross margin—

Steve Tabb: We know that, but how much lower? I mean, I think it's about, what, 10 or 12%? Twenty percent lower, so it adds a tremendous amount. And if you even have to borrow some money from the bank, what do you pay, 5 or 6%? I'd like to see you borrow a lot, but I can see you increasing your wire production without borrowing. And if you're happy, you would borrow a little and you would be making a heck of a lot more.

Roy Yu: Yes, and given that, you know, we need to purchase more machines and adding the capacity. So we need more room, that's number one; but currently—in our current facility, if you come visit us, you can see all buildings are full up so we don't have any further space to fill in any more drawing machines. And on the new facility currently, the reason we built our two new smelters first, is because we have large orders from customers for copper anode. And which—copper anode is the product can use less working capital versus the drawing machines. And we have more room left in our new facility, and going forward we're definitely considering to add more drawing machines.

Steve Tabb: Yes, well okay. I'd like to see more drawing machines. You said you're going to save $150 a ton when you get your licenses and you start importing in more bulk.

Roy Yu: Yes. Currently we're buying from the tweeters, you know, who buy scrap copper and imports—

Steve Tabb: Yes. But my question is—

Roy Yu: We're talking to the middle man.

Steve Tabb: How—based on existing selling prices that you have for anode and the prices that you're paying for scrap, what would $150 a ton increase your gross profit by, percentage-wise—based on the anode? What does it cost per ton now, so that the $150—what percentage would that be on that?

Roy Yu: You mean what percentage will increase the gross profit?

Steve Tabb: Yes, how will it increase—how much will it increase the gross profit?

Roy Yu: Yes, based on today's copper price, it will be about 1.5%.

Daphne Huang: Based on the first quarter, which on the gross profit side I think it's about—it's very significant. It's somewhere between 15 to 18%. That's $150 of increment.

Roy Yu: Yes, that will increase the gross profit by 1.5%.

Steve Tabb: But an increase—I'm confused. Overall, it will increase the profit per ton. What are you—you have profit per ton on anode now, and what is the selling price and what is the cost now on a per-ton basis, so I can see what the $150 is as a percentage? What is your average selling price on your anode now?

Roy Yu: It's about—for the first quarter, the average selling price for copper anode is about $9,000 per ton.

Steve Tabb: Okay, and what was your average cost?

Roy Yu: You mean average cost per ton for the anode only?

Steve Tabb: For the anode only.

Roy Yu: Hold on a second.

Daphne Huang: Steve, your question is concentrated on what kind of percentage improvement on the gross profitability of copper anode, right?

Steve Tabb: Well, yes. What percentage; and then I'm going to try and work it out and how much it's going to affect your gross profit overall.

Daphne Huang: Right. On the anode side, it will be very significant because you're looking at first quarter, let's say the anode average price per ton is about $850 per ton, so that $150 of increment will translate into about 18% of increment on the gross profit for anode. Let's just do a very quick calculation for—

Roy Yu: It's about $8,600 per ton.

Steve Tabb: The cost now is $8,600? No. It can't be. You're selling it for 9,000 and you made a gross profit of only 13% overall, you made even less gross profit on your anodes, right? Your gross profit for the quarter was only 12.7—what was it here? I have it right here. Yes, your gross profit for the quarter 12.3%, and that included—what was the mix? How much of these sales were anode and how much was drawing of the 137 million in the first quarter?

Roy Yu: Yes, Steve let's do this. So we can have another call to discuss all the numbers, and I can give you all the details. Is that okay?

Steve Tabb: Okay, but I'm sure the analysts want to know too. It's up to you! All right.

Daphne Huang: Steve, just quickly let me jump in. I did some calculations very quickly. Assuming, okay, because copper wire and copper anode, they're all sourced from scrap copper essentially in our products. So assuming the same sales quantity of the copper wire and copper anode for the first quarter, and I just put an assumption of additional $150 per ton of benefit from importing—direct importing, that really translates into about 12% of incremental benefit on the first quarter gross profit. And on copper anode alone, if we do the $150 of increment, that will be, again, like I mentioned before, about 18 to 20% of increment. So that is pretty significant. If you translate that, I think we kind of cost in the past, Steve, if you translate that $150 of estimated savings or increment on the gross profit, $150 per ton multiplied by annualized capacity, full capacity, which is going to be 100,000 tons per annum, based on the four smelters running at full capacity, that will really equate to somewhere around $0.33 per share on a fully diluted basis, assuming net income is about roughly two-thirds of.

Does that answer your question?

Operator: Your next question comes from the line of David Rosenfeld of William Jones. Please go ahead.

David Rosenfeld: Good evening. I was wondering if Mr. Zhu could talk about your efforts in product development and the product areas that you're targeting looking ahead.

Roy Yu: [Chinese spoken]

Jianhua Zhu: [Chinese spoken]

Daphne Huang: Mr. Zhu just provided some updates on the new product side. One of the new products that we're doing R&D on, is basically in the CTA wire side of products. Hopefully that, you know, if that becomes reality, that's going to answer your question. We are committed to expanding capacity in the higher margin, higher profitability business. But going back to Mr. Zhu's comments, this new product is very exciting. It's going to be in the—contributing to the power cable side of the industry. It's going to be—once it's successful, it's going to be really the first product in that power cable industry, which is substituting the pure copper wire currently being used in the industry. Essentially, this product is going to be—going to have about 50% of copper on the outside and 50% of aluminum on the inside. Once that's successful, we—our product testing is obviously ongoing, but once that's successful it's going to be able to replace almost all of the power cables in, for instance, in the development in the rural area, which there is some—a lot of room for expansion down the road. So that's very exciting.

And also, Mr. Zhu just disclosed that right now, we got reverse inquiries from a wind power company in the U.S., actually. They are just waiting for this product to be tested and got all the licenses, and the potential customer, actually, from the U.S. is very excited and they wanted to purchase our product once that matures. So that's very exciting news.

David Rosenfeld: So what do you think the timeline is for something like that, and maybe just comment a little bit about what the actual differential and the cost saves to the customers might be?

Roy Yu: David, this is a brand-new product so currently CCA are not used in power cable industry. So by using this kind of product, it's going to save our customer up to 40% of cost. But, you know, currently we're still in the R&D process so we cannot give any timeline. But hopefully in year 2012 or 2013, we can have this new product sales to market.

David Rosenfeld: All right, thanks.

Operator: Ladies and gentlemen, your final question today comes from the line of Steve Emerson with Emerson Investment Group. Please go ahead.

Steve Emerson: First of all, congratulations on a great quarter. While you don't know the timeline for the new product, what is the typical testing period to get qualified for a new cable like this in China, and when—what timeline would it be to submit the cable for certification and testing?

Roy Yu: Well Steve, first of all, these are brand-new products so it's not kind of to have—like the import license, to have a certificate from the government. It's going to involve a lot of testing process, so it's really hard for us to giving out a timeline because we are not in control of that.

Steve Emerson: No, I understand that. I'm asking what would be the typical timeline for testing of a product like this. Is this a year? Is this six months? What is it?

Jianhua Zhu: [Chinese spoken]

Daphne Huang: Mr. Zhu gave a little more detail—

Jianhua Zhu: [Chinese spoken]

Daphne Huang: Okay. Mr. Zhu just gave a little more detailed explanation in the new product process. In terms of our particular new product, we have already spent over a half year in the R&D, and it will take—typically, he said the process will take somewhere between about two years of—from, you know, R&D to getting our product resistance test, and we have to start—once we start production—once we pass the resistance tests, we cannot start production right away in full capacity. We have to all of, like, do test batches before [inaudible]—and test another round of test [inaudible] before production. So given the timeline, it looks like we already spent over more than half a year of timing, so you'll look—short to the long is you'll look about a year and a half kind of timeframe, when we get the standard certification, everything from the national authority.

Steve Emerson: Thank you. You said to a previous caller that your gross profit per ton for anode was $850. What was the profit per anode ton—gross profit in Q4, and could you go through your other two business segments—what the gross profits per ton were in the quarters versus Q4?

Daphne Huang: Steve, we'll be able to give you a very accurate breakdown if we need to after the call, but for the first quarter—actually the fourth quarter, for anode fourth quarter gross profit per ton was about $750. The first quarter, actually, we were better in the gross profit per ton. It was about $850 per ton. On the other two products in the first quarter, my rough estimation—obviously we haven't given sort of detailed breakdowns on the wire products, but rough estimation on the copper wire side is about somewhere around $1,200 per ton. On the CCA wire side, it's about $3,500 per ton.

Now, one thing that I want to mention to everybody is the fluctuation in average gross profit per ton on our products, on our wire products, obviously depending on the type of customer orders blended comes in. For instance, if there are more thicker wire orders in terms of percentage, then obviously it will bring down the blended gross profit per ton for the wire products.

Steve Emerson: And for comparison purposes, would you give Q4 quickly if you have it handy?

Daphne Huang: Sorry, Steve?

Steve Emerson: Q4 profit per ton in wire and CCA?

Roy Yu: Steve, we can give you the detailed numbers after the call. We're going to email you all the numbers you want, okay?

Steve Emerson: Thank you very much.

Jianhua Zhu: Thank you.

Operator: As there are no further questions at this time, I will turn the call back to management for any closing remarks.

Daphne Huang: Thank you once again for joining us on today's call. As we enter new periods of growth, we invite you to follow our progress as we look forward to what lies ahead. If you have any further questions or need additional information on the analyst day and investor day on May 24, please do not hesitate to contact our investor relations partner at the Piacente Group. On behalf of Mr. Zhu, Roy and the rest of Lihua's management team, I would like to thank you all for your continued support. Thank you.

Operator: Ladies and gentlemen, this concludes the Lihua International Q1 2011 Earnings conference call. This conference will be available for replay after 10:00 am Eastern time today through to May 17, 2011 at midnight. Thank you for your participation and you may now disconnect your line.

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