

Operator: Greetings, and welcome to the Helios Technologies Third Quarter 2021 Financial Results Conference Call. [Operator Instructions] As a reminder, this conference is being recorded. I would now like to turn the conference over to your host, Tania Almond, Investor Relations and Corporate Communications for Helios Technologies. Please go ahead.

Tania Almond: Thank you operator, and good morning everyone. Welcome to the Helios Technologies Third Quarter 2021 Financial Results Conference Call. We issued a press release this morning, if you do not have that release, it is available on our website at hlio.com. You will also find slides there that will accompany our conversation today. On the line with me are Josef Matosevic, our President and Chief Executive Officer; and Tricia Fulton, our Chief Financial Officer. They will spend the next several minutes reviewing our third quarter results; discussing our progress with our accelerated growth goals; updating our Outlook for the rest of 2021 and then we will open the call to your questions.

If you turn to **Slide 2**, you will find our safe harbor statement. As you may be aware, we will make some forward-looking statements during this presentation and also during the Q&A session. These statements apply to future events that are subject to risks and uncertainties, as well as other factors that could cause actual results to differ materially from where we are today. These risks and uncertainties and other factors will be provided in our 10-Q to be filed with the Securities and Exchange Commission. You can find these documents on our website or at sec.gov.

I'll also point out that during today's call, we will discuss some non-GAAP financial measures, which we believe are useful in evaluating our performance. You should not consider the presentation of this additional information in isolation or as a substitute for results prepared in accordance with GAAP. We have provided reconciliations of comparable GAAP with non-GAAP measures in the tables that accompany today's slides.

With that, it's now my pleasure to turn the call over to Josef.

Josef Matosevic: Tania, thank you, and good day everyone. Please turn to **Slide 3** and I will summarize our highlights for the quarter.

Our Helios team delivered outsized growth again this quarter across each line of our business by expanding our market share with our current customers, winning new customers, and diversifying the markets we serve. We believe this is a direct result of the strong execution on our augmented strategy for growth that is made possible by the passionate culture instilled in our team with shared values of integrity, inclusion, leadership, accountability, and innovation.

Every day we leverage our core values as we address the challenges of supply chain constraints and material costs head-on with flexibility, agility, and creativity. We are not immune to the logistical constraints everyone is facing with transportation challenges. We are prioritizing constantly to meet our customer's needs by partnering with our suppliers and identifying new sources to complete orders timely and maintain our top-tier lead times.

We have stayed focused on optimizing our manufacturing efficiencies and implemented multiple pricing strategies across our businesses to cover the inflationary pressures being realized. It's important to note that through all of this, demand remains robust across all our markets, and we believe we continue to take market share due to our responsiveness to our customer's needs.

In fact, we had 30% organic growth in the quarter reflecting strong demand and our operational flexibility to deliver. This was bolstered by winning new customers in diversified markets as well as the new products we have introduced that are being well received.

Additionally, we recently won an important new customer in the electric vehicle design and manufacturing space. We will provide edge-to-edge electric control displays over a multi-year period. This is a perfect example of a new customer win in a diversified market.

As you know, this quarter we have been integrating our NEM acquisition that I spoke about on our last call. We are very excited about how nicely we see their products filling out our good, better, best portfolio approach in our electro-hydraulic product offerings. We expect to start bringing these combined offerings to the market relatively quickly through the end of this year into early next year.

Just after the third quarter ended, we closed our acquisition of the assets of Joyonway. Both NEM and Joyonway are excellent examples of the effectiveness of our flywheel acquisition strategy.

Joyonway is an ideal addition for our Electronics segment. They complement our controls platform from our Balboa acquisition, further expand our reach into Asia, increase our manufacturing capacity, as well as help us better service 'in the region for the region', and strengthen our supply chain. They are another example of a strong standalone business that fits within the Helios business system like a glove and we will be able to create a multiplier effect.

Because of our strong cash generation this quarter, we have once again rapidly de-levered our balance sheet quickly getting back to our target two times (2x) leverage metric providing dry powder to continue advancing our acquisition strategy. And I should add that the pipeline continues to remain very robust.

Due to the strong quarter performance, the strength of demand in our markets and our team's excellent work on achieving manufacturing efficiencies, we are again raising our full year 2021 revenue and non-GAAP cash EPS outlook while holding margins steady even with the backdrop of this most unusual operating environment in the supply chain.

We are encouraged by what we are hearing from our customers and believe this sets us up for a solid 2022 as well.

Let me review some financial highlights on **Slides 4 and 5** and then pass it over to Tricia for more details.

Our second quarter net sales increased over 80% to \$223 million including \$64 million in sales from acquisitions. Our adjusted EBITDA margin remains top tier performance at 25.1 percent. This was a 170-basis point expansion over last year.

Non-GAAP cash EPS was \$1.07 more than double over last year, reflecting the strength of the economic recovery, our ability to capture a greater share of growth, and the addition of several excellent acquisitions.

Our Helios team is the absolute key to our success, and I could not be prouder of their dedication and fortitude through the most unusual operating conditions of probably all our careers.

I will now turn the call over to Tricia to review the financial results and outlook in a bit more detail. Tricia?

Tricia Fulton: Thank you Josef, and good morning, everyone. On **Slides 6 and 7**, I will review our third quarter consolidated results.

As Josef noted, we outperformed and delivered outstanding growth in the third quarter supported by our focus on delivery lead times and managing our operations efficiently. We continue to expand our sales channels while our existing end markets remain robust.

We are focused on executing our flywheel acquisition strategy and our most recent transformative acquisition of Balboa exceeded our expectations again.

Net sales grew 82% over the prior-year period as we executed our growth plans and continue to take market share. As Josef mentioned, we delivered very strong 30% organic growth during the quarter.

Third quarter gross profit of \$80.9 million increased \$34 million, or 72%, over the prior-year period from higher volumes. Gross margin was a very healthy 36.2% and was impacted year-over-year by the difference from Balboa's margin profile. Throughout the quarter we captured manufacturing efficiencies and improved leverage of our fixed cost base on higher sales, which were offset by increases in logistics and raw material costs.

We have been and continue to implement multiple pricing strategies while also carefully managing the business to overcome the higher input costs. Manufacturing is performing well given the constant reprioritization we need to do to get product out the door. Maintaining extreme flexibility and agility in our operations has been a competitive advantage and is helping us take market share.

Adjusted EBITDA margin grew to 25.1%, up 170 basis points from the same period a year ago, reflecting higher volumes and our disciplined cost management efforts.

Non-GAAP cash EPS improved \$0.54 to \$1.07 for the third quarter over the prior-year period reflecting strong demand across all industries and better-than-expected performance of the Balboa acquisition.

Our effective tax rate in the third quarter was 25.5% compared with 20.7% in the prior-year period due to a reduction in available tax incentives and increased earnings in higher tax jurisdictions such as Italy, Germany, and Australia.

Please turn to **Slide 8** for a review of our Hydraulics Segment third quarter operating results.

Third quarter Hydraulics sales of \$133 million were up 36% over the prior-year period and benefited from broad-based improved demand in most of our end markets showing very strong annual growth in the Americas and EMEA. Annual organic growth in this segment was 31%. Sales included a positive \$1.0 million impact from foreign currency exchange rates.

Q3 Hydraulics gross profit benefitted from higher volume while margin increased 150 basis points to 37.6%, primarily driven by fixed cost leverage on higher sales, manufacturing efficiencies and sales mix.

The 460-basis point operating margin expansion to 23.8% compared with the prior-year period reflects operating leverage on higher volume as well as our disciplined execution on our manufacturing strategy.

Please turn to **Slide 9** for a review of our Electronics segment's third quarter operating results.

Electronics sales were \$89.8 million up from \$24.4 million in the year ago period, reflecting an increase of 268%. Annual organic growth in this segment was 26%. We are seeing strong demand from the health and wellness and recreational markets. Supply chain constraints limited sales in both end markets in the quarter.

Acquisitions contributed \$59.0 million in revenue to our Electronics Segment for the third quarter. Next quarter we will observe one year since acquiring Balboa and it will be classified into our

organic growth category. We continue to be very excited by the potential this acquisition has brought to our business.

Electronics segment gross profit of \$31.3 million in Q3 increased with the acquisition and higher volumes. Electronics gross margin was 34.9% and reflects the impact of mix primarily related to the different margin profile of the Balboa acquisition, as well as increased costs resulting from supply chain challenges to meet strong customer demand.

Operating income for the Electronics segment of \$18.4 million was up from \$4.7 million in the prior-year period and operating margin improved 130 basis points. The 2021 third quarter margin reflects operating leverage gained with Balboa's favorable operating margin profile and higher volume in the organic business.

Please turn to **Slide 10** for a review of our cash flow.

Cash from operations was \$32.5 million in the third quarter, compared with \$36.7 million in the prior-year period. We are carefully balancing our working capital requirements with our efforts to provide timely deliveries to our customers amidst significant demand and material shortages.

For the quarter, capex was \$6.7 million, up from \$1.9 million in the third quarter of 2020. Capex for the full year 2021 is expected to range between \$25 million to \$27 million. This is down from our range of \$30 million to \$32 million due to the timing of when certain investments will be available. On a year over year basis, this will be an increase of 78% from our capital expenditures in 2020.

Free cash flow was a strong \$25.7 million at the end of the third quarter equating to a trailing twelve-month free cash flow conversion rate of 103%. We are confident we have significant financial flexibility to further pursue our flywheel acquisition strategy.

Regarding our capital structure on **Slide 11**, we continue to rapidly de-lever our balance sheet. This quarter we hit our target range of pro-forma net debt-to-adjusted EBITDA leverage of 2.0 times. This improved from the 3.0 times at the end of 2020.

Total debt was \$471 million at quarter end. We also had \$121 million available on our revolving lines of credit with total liquidity of \$169 million.

As a reminder, our financial strategy is to increase leverage for disciplined acquisitions and then generate the cash to quickly pay that down. Our capital priorities remain debt reduction; organic growth through new products and technologies; acquisitive growth and distributions to shareholders. In fact, with our next dividend payment, we plan to join an elite group of public companies that have paid dividends for 25 years straight.

Now let's turn to **Slide 12** and I will discuss our outlook for the rest of 2021.

Our guidance for 2021 assumes constant currency using quarter end rates, as well as the assumption that our markets are not further impacted by the global pandemic.

As a result of our outperformance this quarter, we are raising our revenue outlook for 2021 to the range of \$840 million to \$860 million, which implies an annual growth rate of approximately 63% at the mid-point of the range. We are holding Adjusted EBITDA margin outlook steady at 23.5 to 24.5 percent. We continue to leverage our manufacturing efficiencies to offset stronger headwinds in the fourth quarter due to rising material costs.

This implies we are raising our expectation for Adjusted EBITDA dollars to the range of \$197 million to \$211 million, or a 68% annual growth rate at the mid-point of the range. Additionally, we

continue to invest, through non-capex related items, into our manufacturing strategy to reap the rewards of margin improvement over the long term.

Relative to our margin guidance, we are reflecting inflated material and freight costs continuing through the remainder of the year, the challenges of obtaining parts and supplies even as we build inventory as well as the difficulties in staffing and balancing production lines.

We are tightening our interest expense outlook to \$16 million to \$17 million at current borrowing levels and rates.

The expected effective tax rate for 2021 remains in the range of 22 to 24 percent.

Depreciation is now expected to be between \$21 million to \$22 million, while outlook on amortization is unchanged at approximately \$32 million to \$33 million.

We are raising our Non-GAAP Cash EPS outlook to between \$3.75 to \$4.10 per share, or a 75% increase over the prior year at the mid-point of the range.

The increase in our guidance for 2021 is driven by the strong end market demand we had so far during the year and expect to continue throughout the remainder of 2021. We expect that we can leverage our fixed cost base and maintain our strong margins even given the headwinds on the supply chain, material costs and logistics. The spread in our ranges this far into the year is an indication of the highly unusual operating environment we all find ourselves within.

With that I will turn the call back to Josef for some final comments.

Josef Matosevic: Thank you, Tricia. These are certainly fascinating times. We have exceptional demand for our products while also having to be very agile to meet that demand. Our team has proven we are up to the challenge, and we remain very excited about how we are shaping and driving our future forward!

With that, let's open the lines for Q&A.

Operator: [Operator Instructions] Our first question is from Nathan Jones with Stifel.

Adam Farley: This is Adam Farley on for Nathan. You called out your really strong lead times a couple of times on the call and you called out share gain opportunities as well. Could you provide a little bit more color on what the share gain opportunities have been so far?

Tricia Fulton: Yes. I think we've seen a lot of opportunities on an individual basis coming through from a market share gain perspective, where we have had a customer reach out to us and say, "Hey, I can't get this from one of your competitors," and we've been able to satisfy the need for that customer.

In some cases, it's a one-off, but in many cases, we believe it's a long-term share gain for us. We've seen a lot of those in the Hydraulics space over the last few months; maybe a little bit less on the Electronics side, but part of that is supply chain related, because that's hitting the Electronics side a little bit harder than Hydraulics. We've been able to really maintain our strong lead times on the Hydraulics side and take market share.

Josef Matosevic: And Adam, probably the other data point would be that we had our distribution come from meeting here just about a week ago and that kind of confirms what Tricia just said with the feedback we've received from the distributors, and it's all apparent that there were previous customers who did not purchase from us that we are now supplying. So, those are the 2 key drivers.

Adam Farley: Okay, and do you think there's any double ordering going on in the system with any customers trying to secure inventory?

Tricia Fulton: We don't have an indication that there is any. I mean, right now, everyone is just trying to get what they need, understanding the logistics and supply chain issues, as quickly as possible, but we don't see any indication of double ordering. No.

Operator: Our next question is from Mig Dobre with Baird.

Mig Dobre: Well done in a difficult operating environment. I guess I'm looking for maybe a little more context, Josef, regarding the tenure of demand in your two businesses. I'm curious as to how orders are running relative to revenue. Are you seeing higher or lower order intake in the quarter relative to what you reported in revenues?

I'm also curious, given the amount of disruption that is out there, have you seen any negative impact on customer demand? What are you hearing from your OEM customers as far as how they're planning their own production, not just for the fourth quarter, but really into 2022?

Josef Matosevic: So, in terms of your first question, our order pattern has been very consistent throughout all of our businesses. It really hasn't fluctuated up and down in both segments, Hydraulics and Electronics. You always go through a period of time where you see a spike up, and then, a balance back down; and then, you get quite a few calls and can be actually shipping earlier. And so, you get that type of stuff, but, in terms of order pattern, there hasn't been really any fluctuation or cyclicity.

On your second question, we look at this very closely every single day. When we changed our guidance, we factored that in. There is a strong level of optimism in certain areas, and now, obviously, with the infrastructure bill that passed and will be signed, that optimism has obviously peaked. We are just super careful how we're going to meet the demand. What we're hearing very consistently is that demand should stay robust.

We're working very closely with our distribution and OEM partners to really level out the schedule, so we can fulfill that schedule on a timely basis. The demand is stable. We are seeing upticks in certain areas, and we have balanced this very carefully with some of the supply chain challenges. That's kind of where we are, Mig.

Mig Dobre: Okay. Maybe to put a finer point, looking at your Hydraulics business, the thing that surprised me looking at both EMEA and Asia Pacific is, revenues here are fairly consistent sequentially in the third quarter relative to the second, and we've heard that China has slowed down and equipment volumes are certainly lower there.

In EMEA, that's basically the faster business where there has been disruption for ag OEM customers. I think one of them has talked about having outright planned shutdowns for their European operations.

So, what are you seeing in these 2 geographies, China specifically; and then, the progression of demand for your ag customers and, implicitly, your EMEA Hydraulics business?

Josef Matosevic: On the China piece, and Tricia can chime in as well, I think what really helps us, Mig, is that we really stay true to our strategy of being a niche market in the region, for the region, in Asia. One of our strategic pillars, just a year ago, was to have more of a system solution approach where we have our Kunshan factory not just manufacture and ship hydraulic components, but all the electronics components as well.

So, we were able to have an impact in Asia from a more system cell approach than just a component approach and it helped us in the region with local supply chain and local capabilities of manufacturing.

In EME, if it's Italy, Germany, U.K., Spain, you name it, we have seen very strong and promising demand, with no interruptions. We are seeing cost headwinds in terms of inflationary period, but we knew that would happen and we are offsetting that with price increases.

And as you know, we were successful also in working with the OEMs on price increases, and those went through. But then, we have a lot of flexibility in our European manufacturing to flex labor up and down, and we prebought quite a bit of material to really protect us as much as we can.

Tricia Fulton: Just to add a little bit more specifics on a couple of the markets. In APAC, we are seeing the Korean construction market be very strong and it's picking up speed, which has historically led to then China ramping back up at least from what we've seen historically. And then, China ag is extremely strong in our QRC business as well. They're growing very quickly and taking market share there.

The other part of APAC that is starting to come back a little in the third quarter is the mining in Australia. We have quite a bit of our business there. We had seen a decline because of COVID, where we literally couldn't get into the mines, but now, we're able to go back to those customers, and that seems to be ramping back up as well.

Mig Dobre: That's helpful. My last question, you mentioned pricing and I am curious if we can get a little more detail or context on this. I look at your incremental margins on EBITDA and they've been remarkably consistent - 28%, 29%, 27% - throughout 2021 despite incremental costs, right? You called out transportation, materials, and a number of other factors.

So, I'm curious as to how you've been able to deliver these steady incremental margins. How is pricing looking and what might be the carryover contribution into 2022?

Tricia Fulton: We've been able to get pricing throughout all of the businesses, in some cases, multiple times throughout the year. In addition to that, the manufacturing strategy is really taking off and helping us with manufacturing efficiencies that are driving some of that incremental gain that we're seeing as well.

Mig Dobre: And carryover into '22, can you comment on that?

Tricia Fulton: Some of the price increases went through as permanent and some of them went through as surcharges related specifically to material increases. So, there will be some carryover into '22 and there will likely be additional pricing actions in '22, just related to general price increases.

Operator: Our next question is from Jeff Hammond with KeyBanc Capital Markets.

Jeff Hammond: So, just to follow-on Mig's question, I think he had asked about either book-to-bill or if you're still building backlog here, or if just your ability to ship is allowing you to kind of work that down at all.

Tricia Fulton: We saw a very strong backlog, and that really is coming from the end market demand. I expect that the backlog will be strong headed into 2022. Like everybody else, we do have some past due, but we are doing a very good job at managing our past due dollars right now, and getting them out the door as quickly as we can.

A large majority of those, I would say, are on the Electronics side, where we have some of the part shortages where we're literally missing one part before we can ship something. As soon as those come in, we're able to turn it around. I think the backlog is a testament really to the end market demand.

Jeff Hammond: Okay. And then just to be clear, I think you said you lost some revenue or you had some deferred revenue in Electronics, but that was not the case in Hydraulics. Could you maybe quantify how much you think slipped to the right?

Tricia Fulton: Actually, we saw deferred revenue in both segments as a result of parts shortages or not having the parts on a timely basis.

It takes us some time once they get in the building to be able to build it, turn around and then ship it. We saw some of these parts really freeing up the last couple of weeks of the quarter, but we weren't able to necessarily get everything out the door, and then, it falls into October. I would say, of what we had, about 2/3 of it is Electronics and 1/3 is Hydraulics.

Jeff Hammond: Okay; and then, just a last one. As we look into fourth quarter, should we think of the step down in revenue and margins as seasonal or is there something more there?

And maybe, particularly on the margins, is there something getting particularly worse there? Because again, my model kind of shows the same thing, like incrementals, being pretty consistent through the year.

Tricia Fulton: Given everything that we're seeing on the supply chain side, we've been cautious with Q4, recognizing that it's going to require a very strong flow of products or components coming in the door to ship. Along with that, clearly, in Q4, there's always some seasonality that's related to less shipping days due to holidays, specifically in North America and EMEA.

So, it's probably a little bit of both, I would say, but I don't think there's anything that you need to read into that other than those 2 items, supply chain and normal seasonality for holidays.

Operator: Our next question is from Josh Pokrzywinski with Morgan Stanley.

Josh Pokrzywinski: Josef, you've mentioned the share gain and folks who can't get supply from a traditional supply base seeking you out and you being able to fill in on that.

I'm wondering how do you see that evolving going forward? I mean, I would imagine that all those customers, including your own core customers, are trying to validate backup suppliers just in case? Do you think that there's some sort of normalized middle ground where they spread it more evenly between yourselves and maybe their historical supply base or do you think you're winning more where it may be a spec-in application where they would just go with you from now on - as this all blows over, of course?

Josef Matosevic: So, a couple of things, Josh. As we said before, we invested in our own destiny here, knowing that the supply chain constraints will and should happen. And so, we had a lot of folks within our key competencies, suppliers actually work with them hand-in-hand.

And then, we also developed our internal capabilities with our make versus buy strategy, meaning as we acquired new businesses, we didn't only acquire capacity but also capability. Once we fully flushed this out, it clearly made sense that there are certain core competencies that we can manufacture internally, not just much quicker, but also much more cost effective, and it can flow through our process accordingly.

So, all this combined got us to a point where we're in a position to hold our lead times very steady and meet our demand with our customers.

But then, at the same time, with our diversified market strategy where we worked and targeted three customers within each of our business units under Electronics and Hydraulics, and that process has begun very strongly. And now, we're in a position where we won a couple of them. We also announced another one today that's going to carry out over the next 5 or 6 years.

All in, we do believe we will have an advantage as a company in terms of our lead times, but also from a cost structure standpoint as we will not be as dependent as we were once before, a couple or 3 years back.

So, we've taken the proper steps as we have announced it in our investor meeting. Tricia, on your part?

Tricia Fulton: No, I think you've covered it.

Josh Pokrzywinski: And then, maybe taking a step back, how have you seen book-to-bill lay out through the year, and how do you feel about backlog seasonally with pull-ins versus pushouts on customers taking delivery?

Again, organic growth has been really strong all year here. I was just wondering if the sequencing or backlog position has changed at all as you have passed through the year.

Josef Matosevic: Yes. I mean, look, demand remains very robust, pretty much in both of our segments. There hasn't been an issue. In terms of pull ahead, I think we are focused on shipping exactly what the customer needs right now, so we really don't experience or have any mortgaging of other quarters, so to say. So, we don't have that going on.

In terms of orders going forward, we are really super excited about how 2022 could shape out. We are, by nature, a very humble and conservative company, so our visibility in the Hydraulics segment is only a couple or 3 weeks. Our visibility in the Electronics segment is a little broader. As long as we can mitigate our supply chain constraints that the world is facing, we should have a pretty decent 2022.

So, the backlogs are strong in both segments. Nothing has been mortgaged and we're trying to fill in the demand but also stay very, very methodical and disciplined, not by overcommitting and under delivering. So, our shareholder value here is pretty lucrative going to 2022, I would say.

Operator: [Operator Instructions] Our next question is from Jon Braatz with Kansas City Capital.

Jon Braatz: I have two questions. Number 1, obviously, this morning, there's a lot of buzz surrounding the infrastructure bill. When you speak with your customers, can you help sort of separate reality from the hope and the expectation on this bill? Could it prove incremental to the demand that you're seeing in 2022 or is it just going to be more of a longer-term issue?

Josef Matosevic: Well, I think in our area of the niche market, Jon, there's clearly an opportunity for incremental volume, what we have been discussing with our OEM customers, what the supply constraint looks like from an overall product offering.

We may be on time, and we may be delivering the products and so many others as well, but what is the total impact that they're experiencing currently? That's what we're trying to learn, Jon. In terms of your question, we do see this as incremental opportunity for us.

Jon Braatz: In 2022?

Josef Matosevic: Yes.

Jon Braatz: All right. And then, secondly, over the last couple of quarters, Balboa's revenues have been sort of sequentially flat. Are you seeing the favorable impact from the pandemic on their revenues beginning to abate? Are you seeing any change as it relates to the pandemic?

Josef Matosevic: So, I think what that relates to, Jon, is more at the electronic component shortages. Once again, our order pattern has been very robust and, let me tell you, we could have shipped a lot more product. Like Tricia said earlier, we have a week that we kind of go hand to mouth; and then, in the last couple of weeks of the quarter, the products starts flowing nicely, but you run out of daylight.

So no, we have not seen a stoppage or a slowdown yet. We certainly hope with our augmented strategy on diversifying the market and the acquisition of Joyonway, we will be able to penetrate the product line into many more other markets. If the supply chain maintains where it is right now, we should be pretty good.

Operator: We have reached the end of our question-and-answer session. I would like to turn the conference back over to Josef for closing remarks.

Josef Matosevic: Thank you, operator. Thank you all for joining us today. As always, we certainly appreciate your interest in Helios, and look forward to updating all of you on our fourth quarter next year. We remain super confident in our ability to continue to grow and deliver value for all of our stakeholders. Have a great day and stay healthy.

Operator: This does conclude today's conference. You may disconnect your lines at this time and thank you for your participation.