Tania Almond

Thank you, operator, and good day everyone. Welcome to the Helios Technologies Third Quarter Financial Results Conference Call. We issued a press release announcing our results yesterday afternoon. 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 Sean Bagan, our Chief Financial Officer. They will review our third quarter results along with our updated outlook for the remainder of 2023. We will then 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 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 have been provided in our latest 10-K filing as well as our upcoming 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. Please reference **Slides 3 through 6** now.

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

Josef Matosevic

Tania, thank you, and welcome to today’s call. I want to take a moment to send our heartfelt sympathy to everyone being impacted by this new conflict in the Middle East. We are all living through very tenuous times.

Shifting to the business, let me start by welcoming Sean to his first quarterly call with Helios. Sean joins us most recently from Polaris where he spent 23 years advancing through their global ranks. He has a proven track record of building, growing, and transforming global businesses into highly productive and profitable operations. Sean has hit the ground running and is a great fit with our team and our company values.

He joins us at a very important time as we faced a dramatic shift in market dynamics this quarter. I would like to thank the Helios team for their tenacity in navigating these challenging conditions, while maintaining focus on our long-term goals.

We saw positive trends starting this year. Last quarter, signs of stalling started to show. As we advanced through August and September, they took a turn. As I noted on our last call, our near-term visibility is in fact less clear than our long-term outlook.

EMEA shows signs of weakening before it improves. The U.S. economy has pockets of softness. The APAC recovery is taking longer than even that region, especially China, had expected. Our customers in the Americas, currently representing 55% of total revenue, are beginning to hesitate. Those customers are facing a less favorable environment for consumer spending and financial liquidity. This equates to what the Fed has been pushing for, a slowed economy to tamp down inflation.

Given current conditions, we have been taking proactive actions to protect our margins by optimizing our cost structure while balancing our resources to deliver the top-notch service our customers have come to expect.

Even with global macroeconomic and geopolitical uncertainty, I am confident our strategy is intact. While we manage through the short term, we must continue to lead and execute for the long-term. For the last several years, we have been methodically investing for growth. We are well positioned to be able to drive significant leverage across the top and bottom lines when the markets start to recover.

We are encouraged with the progress we are making across several customer projects we described last quarter. All these deals are still in play. The timelines or decisions on some have been pushed out based on the macro. Those customers are facing near-term challenges but remain opportunistic and committed. Most of these projects are currently expected to begin in 2024 and start to show contributions in the latter half of the year.

We continue to demonstrate that our innovation and engineering excellence are paramount. For example, we recently announced two advanced new products from our electronics segment both with initial customer examples. The first being the PowerView™ P70 and most recently Clim8zone II. We are also building on the value our acquisitions bring to create revolutionary technology. We recently introduced remote support software by integrating i3's capabilities with its Cygnus Support Platform into our OpenPV™ software. Together this creates a solution that will increase end-user satisfaction and loyalty, improve customer support, and enable a recurring revenue stream to capture this added value. In fact, our i3 team has created a software platform for a commercial food service customer who has added the software to thousands of their units. This same customer intends to also leverage the Cygnus platform as it will connect directly with this new software. We are seeing traction with our new products and services; it is just being masked now by the macroeconomic impacts I described.

I will now turn the call over to Sean to review our financial results and updated outlook and then he will hand it back to me for closing remarks.

Sean, please.

Sean Bagan

Thank you, Josef and hello, everyone. I'm thrilled to be here. As most of you know, I joined Helios as CFO on August 9th. In my first 87 days, I had the opportunity to visit all our major operations while meeting a great number of our global team. I am impressed with the strength of our leadership, and believe we have the right strategy to continue to grow the business and leverage our diversification across markets, geographies, and products. We have strong brands, leading market positions, and expansive manufacturing capabilities. These span across processes that range from injection molding, heat processing, wire harnessing, precision machining, through to circuit board printing. We are nimble and responsive, and Helios has a culture of excellence grounded in a strong value system. Combine this with our regional manufacturing capabilities and low-cost operations and I believe it is clear how our strategy to innovate with integrated solutions, including remote service through software systems, makes us very tough to follow.

We are starting from a very solid foundation from all the investments we have made as we further optimize our cost structure. This enables us to weather near-term challenges and be well positioned to capture compounding effects of driving leverage across our business as conditions improve.

Let me start with a review of third quarter results talking to **slides 7 through 13**. I believe the slides speak for themselves and provide quite a bit of detail, so I plan on hitting on some key points and providing additional color.

The surprise factor in our results for the quarter was most visible in the $26.2 million, or 12% sequential sales decline from the second quarter of this year. Demand in the third quarter reflected a rather swift change in dynamics as certain customers − across mobile, agriculture, marine, industrial, and health and wellness end markets − shifted gears and began pulling back orders and pushing out decisions. Given we have quite a bit of book and bill business, this readily impacted the third quarter.

Every region was down sequentially this quarter, the exact opposite of what we saw in the first and second quarters. European markets were especially weak across both segments and were down 24% compared with the second quarter, or $13.8 million, more than half the total decline. The Americas were down 7%, or $8.7 million, sequentially, while APAC was off 8% or $3.7 million.

The lower volume in the quarter heavily impacted gross profit and margin year-over-year and sequentially due to under absorption. Gross profit declined $9.6 million and gross margin contracted 380 basis points year-over-year. While we had benefits from pricing and foreign exchange, it only partially offset the volume impact along with inflationary costs. Given the larger decline in volume sequentially, gross profit was off $16.1 million from the trailing second quarter resulting in gross margin of 29.6%.

The $6 million increase in SEA expenses compared with Q3 2022 primarily relates to acquisitions, integration, higher wage and benefit costs, along with increased R&D investments to maintain our leadership positions. As evidenced with our actual Q3 2023 sequential reduction of SEA expenses, we are executing plans to control overhead expenses while continuing to position the business for the opportunities we have to continue to diversify and grow.

Adjusted EBITDA in the quarter of $35.6 million, or 17.7% of sales, reflects the impact of volume and investments. Volume is significant for the business as our decremental margins run at about 40%. Our strategic plans are focused on improving our incrementals while reducing our decrementals. I see opportunity to leverage fixed costs as we gain new customers in new markets, while also continuing to gain efficiencies from our integrated manufacturing and operating strategy.

Our effective tax rate in the third quarter was 30.5%, up 690 basis points from 23.6% in the prior year based on the mix of earnings in various jurisdictions.

Diluted Non-GAAP cash EPS of $0.44 in the quarter reflects the impacts I've discussed as well as a 9-cent impact from higher interest expense compared with last year.

Briefly by segment, On Slide 12, you will find the third quarter review of our Hydraulics segment. Sales were up 1%, over the prior year period driven by sales to the Americas and some pricing. We estimate about $7.8 million in sales were delayed due to the supply chain shortages. This started to come down sequentially compared with last quarter. Sales declined to the mobile, industrial and agricultural end markets. Acquisitions added $11.0 million and there was a $2.2 million favorable foreign exchange impact this quarter.

Sequentially, Hydraulics declined $20.4 million driven by swift changes in the mobile, agriculture, and industrial end markets. Notably, of those markets on a year-to-date basis Agriculture is still up − which only intensifies the degree of unexpected change in demand this quarter. The decline is readily seen by region, with EMEA being down $12.5 million quarter-over-quarter, more than half of the overall decline.

Gross profit declined $5.4 million year-over-year resulting in gross margin contracting 430 basis points as pricing and efficiencies were not able to offset flattish volume, the different margin profile of acquired businesses, restructuring costs, and higher wage and benefit costs. Sequentially, gross profit was down $8.6 million, although gross margin contracted just 150 basis points.

SEA expenses increased by $5.6 million year-over-year. The increase was driven by incremental SEA from acquisitions as well as inflation with labor and operating costs and investments in R&D. Sequentially, SEA was unchanged.

Please turn to **Slide 13** and we'll discuss the Electronics segment. Given its U.S. sales concentration, there was no foreign currency impact in the quarter for the segment.

Year-over-year, electronics sales declined $6.6 million, or 9%, and had about $3.4 million in sales delayed due to the supply chain.

Marine, which has held fairly steady in sales every quarter for the last 2 years, had a drop off this quarter impacting both the year-over-year and sequential comparisons. Notably, another category in our recreational market (off-road vehicles) mostly offset the decline in marine. This does validate our diversification strategy is working. This quarter we broadly had so many markets impacted at once our diversification was not able to overcome the macro drag.

Health and wellness was down over 20% year-over-year and 8% sequentially, but still up over 50% from the trough in the fourth quarter last year.

Gross profit was off $4.2 million from lower volume while gross margin contracted 320 basis points as pricing and efficiencies were not able to offset lower volume, higher material costs, restructuring costs and reduced leverage of our fixed cost base.

SEA expenses increased 22% compared with last year which included incremental SEA from acquisitions, increased personnel costs and investments in R&D. Sequentially, SEA grew 2%.

Please turn to **Slide 14** for a review of our cash flow. We generated $11.8 million in adjusted cash from operations.

CapEx of $5.9 million was 3% of sales for the quarter, as investments in capacity expansion in North America and Asia are essentially complete and equipment purchased.

Trailing 12-month Adjusted Free cash flow was $53.1 million with a conversion rate of 103%.

Turning to **Slide 15** even as we face headwinds, we have an extremely healthy balance sheet and the financial flexibility to execute our strategy for growth. Helios' track record of delivering exceptional margins drives its strong cash flow engine. Our capital allocation framework prioritizes dollar one to be invested back into the business to support new product development and operational efficiency. Our longstanding dividend is an important component to overall shareholder returns. Finally, we remain opportunistic on executing both flywheel and transformational acquisitions that fit strategically into the Helios portfolio. Cash and cash equivalents were $35.2 million, providing us sufficient liquidity. Total liquidity at the end of the quarter was $219 million.

We reduced debt by $4.6 million in the quarter and our net debt to adjusted EBITDA leverage ratio was 2.98x ending the quarter.

In summary, while our near-term outlook is less than expected from the start of the year to now, I am extremely encouraged with the underlying strength of our foundation and strategy, the boundless white space of opportunity, and the prospects around creating more discipline to prioritize investments that will produce shorter payback and higher returns.

Turning to **Slide 16**, we'll talk to our updated expectations for the remainder of the year. I will start by saying we have an opportunity to further our discipline around financial forecasting processes through greater rigor of data analytics and leveraging the power of Business Intelligence. Our updated outlook considers the rather swift change in demand we experienced in the third quarter and the feedback we are receiving from our sales channels and customers.

Having been abruptly impacted by global macroeconomic uncertainty and the resulting dynamic market conditions, we are modifying our outlook appropriately for the remainder of the year.

We now expect revenue in the range of $820 to $835 million, implying the fourth quarter revenue of approximately $178 to $193 million. With the decline in volume and the impact to margins combined with continued disciplined investments, we are moderating our adjusted EBITDA targets for this year to $152 to $167 million. I believe our business can support delivering mid-twenty and better Adjusted EBITDA margin over time with sufficient volume. In the near term, our focus is on executing on our long-term strategy while protecting margins and controlling expenses in our operations. We have several significant projects underway that should start to materialize in more meaningful ways later in 2024 and build through 2025. Though we expect with current market conditions, 2024 will start off slower than we had earlier anticipated.

Like my experience at Polaris, where I was involved in the growth of the company from $1 billion to nearly $10 billion, I believe that as Helios continues to execute on our solid strategy while improving our processes and systems, we can grow well beyond the next milestone of $1 billion in revenue. While the near term has macro headwinds, Helios is positioned well to weather these market fluctuations with its expansive end markets, innovative products, diversified geographies, leading market positions, strong brands, and extensive manufacturing capabilities. We have significant potential, and our long-term future is very bright.

So let me turn it back to Josef who will reference **Slides 17 to 18**.

Josef Matosevic:

Thank you much, Sean. Again, we are very happy to have you on the team.

These are certainly interesting times. When I look at what Helios has been able to accomplish together over the last three plus years, I am incredibly proud of the team's hard work and dedication. You can see from the last couple slides we have a great foundation of established step level growth that we are building from. When I think back to 2019 going into 2020 when the pandemic started and there was a market pull back, no one knew exactly what could be accomplished in the near term. You can see how much we have grown since then. We are so much better positioned today from all the investments we have been making the last several years. This is why I am more excited today than I have ever been thinking about our ability to jump up to that next step on the growth scale.

When you think about how we have been transforming into an integrated operating company that could start to generate recurring software sales as early as next year – that is really true transformation.

We have a great future in front of us. We will navigate through this just as we got through the pandemic. We have a proven strategy, a dedicated team, and are excited to keep driving toward our goals every day!

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

Note: Please refer to the webcast version of the call, which is available on the Company's website (heliostechnologies.com), as well as to information available on the SEC's website (www.sec.gov) before making an investment decision.