

Tania Almond, Vice President, Investor Relations and Corporate Communication

Thank you, operator, and good day everyone. Welcome to the Helios Technologies Fourth Quarter 2023 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 fourth quarter results along with our outlook for 2024. 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 those presented today.

These risks and uncertainties and other factors will be provided in our upcoming 10-K 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, President and Chief Executive Officer

Tania, thank you, and welcome everyone.

We delivered as recently committed for the fourth quarter. 2023 is now in our rear-view mirror. As many of you know, we started this journey to transform our business into an integrated operating company several years ago. As I reflect on 2023, it was a year of solid progress along with several macroeconomic challenges and geopolitical events. We kept our focus through it all and emerged as a more united and determined team. We continued to advance our strategy by remaining centered on three key elements.

First, one of our major priorities were the investments we consciously made in our manufacturing strategy. We expect they will drive operational excellence and position Helios for the growth opportunities we see before us. We invested in our Centers of Excellence by consolidating workflows and expanding capacity to address new business and broaden capabilities. As part of these activities, we relocated various operations and functions. The outcomes will increase efficiencies, provide the backup capability needed to further manage risk, as well as expand lower cost regional manufacturing in India and Mexico. Our two North

American Hydraulics Centers of Excellence were fully operational starting in the fourth quarter, and we just opened our new Electronics facility in Tijuana. We are finishing up the process to expand our capacity in Italy, where Faster just reached record sales levels for full year 2023! All these investments were critical for our future, even as it somewhat impacted on our financial results for the year. We believe over the long-term this strategy will maximize shareholder value.

Second, we executed on our strategy to fill product and solution gaps, diversify revenues, and to build out our talent pool with acquisitions. With the addition of Schultes and i3 to add to our string of flywheels, we have assembled a collection of premium capabilities that make us incredibly tough to follow.

Third, we continued our efforts to further diversify our markets and deepen our reach into existing ones. Even in the face of significant macro headwinds, we made the necessary investments in innovation and product development. We are solving customers' most difficult design and production problems increasingly with integrated system solutions. We are well positioned to serve these opportunities which we expect can be significant growth contributors and will help define our future.

Our transformation is nearly complete at this point. Now it is all about execution as we continue to elevate into a global integrated operating company.

Realizing the market challenges we faced in the second half of last year, we took necessary actions to help protect the business. Lower volume clearly had the largest impact on our margins. We recognize the decision to continue our investments in the business and the minor disruption from standing up the Centers of Excellence also contributed. Sean will talk more about our results as well as our financial priorities and our outlook for 2024.

Sean, I will turn it over to you now, please.

Sean Bagan, Chief Financial Officer

Thank you, Josef and hello, everyone.

Before I discuss our financial priorities for 2024, let me start with a review of fourth 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.

Sales came in at the higher end of our most recent expectations for the quarter and the year due to stronger results from Balboa and a quicker catch up on Hydraulics backlog. Compared with last year's fourth quarter, we had a 4% improvement in the Americas, a 10% decline in EMEA, and a 5% decline in APAC (which continued to be driven by softness in China).

As we cited on our last earnings call, the swift shifts we saw across several markets persisted, although we did see year over year growth in health and wellness in the fourth quarter for the first time since 1Q22, granted the comp is off the low water mark. As a reminder, that market had a correction from its pandemic highs and contracted year over year during the first three quarters of 2023. Our industrial, marine, and recreational-based markets had some rapid shifts in the third quarter of 2023, also impacting the fourth quarter.

Sequentially, while Hydraulics was modestly improved, Electronics declined across several categories.

As expected, lower volume in the quarter heavily impacted gross profit and margin year over year and sequentially due to under absorption. Gross profit declined \$7.9 million and gross margin contracted 360 basis points year over year to 28.6%.

A testament to our efforts to contain margins erosion was the \$2.5 million, or 7% decline of SEA expenses compared with the trailing third quarter. The \$35.2 million of quarterly SEA expenses was our lowest level in the year despite the run-rate addition of the two acquisitions in the first half. Our focus was on looking at what I define as flexible expenses – or those that can be deferred, without impacting our strategic imperatives. Year over year, the SEA expense was only modestly higher despite acquisitions.

Adjusted EBITDA in the quarter of \$32.3 million, or 16.7% of sales, reflects the impact of lower volume and investments offset by our cost reduction initiatives. Volume is significant for the business as our decremental margins are being exacerbated where we have expanded capacity. As volume starts to return the positive operating leverage will show up.

Our effective tax rate in the fourth quarter was 23.3% and 23.8% for the full year. This is driven by the regional mix of different tax jurisdictions.

Diluted Non-GAAP EPS of \$0.38 in the quarter reflects the impacts I've discussed. It also includes an eight-cent impact from increased interest expense from higher interest rates and average debt balances compared with last year.

Briefly by segment, on **Slide 12**, you will find the fourth quarter review of our Hydraulics segment. Sales were down 5%, over the prior year period. Sales were down across several end

markets as we cited the swift shifts we saw in the third quarter. We also saw channel inventory data take a small step up from the declines we had been seeing.

We estimate about \$4.2 million in sales were delayed due to supply chain shortages, improving again sequentially, which has leveled back to a more normalized range. We do not plan to continue to breakout this metric going into 2024 unless it becomes more impactful again. We had a \$1.6 million favorable foreign exchange impact to the segment compared to the prior year period. Sequentially, Hydraulics modestly improved by \$1.7 million.

Gross profit declined \$7.4 million year-over-year resulting in gross margin contraction of 390 basis points as acquisitions and pricing did not fully offset lower volume, restructuring costs, and higher wage and benefit costs. Sequentially, gross profit modestly increased while gross margin contracted 30 basis points.

SEA expenses declined sequentially \$1.5 million or 7% compared with the third quarter. Our cost containment measures helped to overcome the run-rate impacts of acquisitions, as well as inflation with labor and operating costs while maintaining our investments in R&D.

Please turn to **Slide 13** and we'll discuss the Electronics segment. Given its U.S. sales concentration, foreign currency has nominal effects for this segment currently.

Year over year, electronics sales improved by \$3.9 million, or 7%, including \$2.3 million in revenue from acquisitions. Approximately \$3.2 million in sales were delayed due to the supply chain, which also declined in this segment sequentially.

As we cited last quarter, several markets had rapid shifts in order timings that impacted fourth quarter with sales down 14% sequentially. Though, health and wellness was up double digits year over year. We have been encouraged by the trends we have been seeing in health and wellness so far this year. We expect to have now lapped the tougher comps and are planning to deliver growth once again in that end market.

Material costs, under absorption, and sales volume and mix impacted gross profit which was down \$500,000 year over year, resulting in gross margin contraction of 260 basis points.

SEA expenses were down 6% compared with last year and down 9% compared with the trailing third quarter. As noted with Hydraulics, we are executing a disciplined focus on cost containment efforts while maintaining R&D investments.

Please turn to **Slide 14** for a review of our cash flow. Given the macro challenges we have been managing through, we are pleased with the free cash flow that was generated during the quarter. We will look to build upon this momentum in 2024. We generated cash from operations of \$33.7 million, our highest level of the year on the lowest top line quarter. This demonstrates disciplined working capital management and strong cash conversion. We had free cash flow of \$25 million in the quarter measurably improved over the prior three quarters in 2023.

Capital expenditures of \$8.8 million was 4.6% of sales for the quarter. This marks near completion of this round of investments in our footprint realignments, capacity and capability upgrades. For the year, capital expenditures was 4% of sales, or \$34.3 million.

For 2023, Adjusted Free cash flow was \$52.3 million with a conversion rate of 139% – the highest it's been in the last three years.

Turning to **Slide 15**...Our balance sheet was stable in the fourth quarter with continued financial flexibility. At year end, cash and cash equivalents were \$32.4 million, and we had \$200.1 million available on our revolving lines of credit providing us ample liquidity as we entered fiscal 2024. While we spent \$34.3 million in capital expenditures and \$114 million for acquisitions, or about \$148 million in investments during 2023, our debt at year end was up just \$79 million. Further, we paid down approximately \$20 million of debt during the fourth quarter.

At year end, our net debt to adjusted EBITDA leverage ratio was 3.01x. We are prioritizing debt reduction in 2024 and moving below 2.5x. Ultimately, as we get closer to the lower end of our two to three times target range we have the ability to flex up for acquisitions and other investments.

Turning to **Slides 16 to 18**, we are providing our initial expectations for 2024. Our estimates do not include the large systems sales projects we have talked about. Once those orders are secured and production schedules agreed upon, we will update accordingly.

For 2024, we expect revenue in the range of \$840 to \$860 million dollars. This represents moderate growth of just over 2% at the midpoint of the range. We expect adjusted EBITDA for the year of about \$163 to \$180 million dollars, for low single to double digit growth. This represents an Adjusted EBITDA margin slightly over 20% at the mid-point of the range. As the markets recover and our volumes grow, our newly expanded capacity utilization will improve resulting in our incrementals driving our Adjusted EBITDA margins to scale over time. Additionally, as we get specked into new system solutions, including recurring software opportunities, these will be very sticky in nature and enable additional accretive margin growth.

With the cost measures we have taken, paired with the non-recurrence of certain items, we expect our net income to improve measurably to a range of \$50 to \$63 million dollars, strong double-digit increases on modest low single digit top line growth.

We expect the first half of 2024 to be tougher on a comparable basis while the back half of the year to increasingly grow on a year-over-year basis.

For the first quarter, we expect sequential top- and bottom-line improvement with revenues likely in the range of \$205 to \$210 million dollars with Adjusted EBITDA margins sequentially improving to approximately 17 to 18 percent.

Looking to **slide 19**, I want to review with you our financial priorities for 2024 that Josef mentioned.

This year is all about execution and driving performance that establishes the underlying financial discipline and structure to deliver returns on our investments.

We have clear financial priorities in 2024:

- (i) Execute on our profitable sales growth plan by realizing operating leverage inherent in our business, while fully instilling investment and cost discipline;
- (ii) Shorten our cash conversion cycle through sustainable working capital improvement initiatives; and
- (iii) Reduce debt utilizing the free cash flow conversion proceeds.

We know execution is critical in delivering on our commitments this year as we strive for more predictable results in 2024. We expect this renewed financial focus will in turn elevate Helios to be the scalable, integrated operating Company into which we are evolving.

With these priorities we expect to deliver continually improving earnings that will drive returns that exceed our cost of capital on the investments we have made.

So let me turn it back to Josef for some closing remarks.

Josef Matosevic, President and Chief Executive Officer

Thank you much, Sean. We appreciate the financial structure and discipline you are embedding into the organization.

I am very encouraged about 2024 and our future. It is about keeping our focus with tenacity on our goals. We are executing our plan and advancing the organization to an integrated operating company that can deliver top tier margins, cash flow and growth. What we have done over the last several years has created the foundation from which we can now elevate. It is thanks to the dedicated, talented people that work for Helios Technologies and its family of companies that we are so well positioned. We are creating sticky, critical, integrated solutions that provide improved productivity and efficiencies with lower life cycle costs for our customers. We are ready...and I believe as markets recover, the next few years look very good for Helios.

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.