Operator: Greetings, ladies and gentlemen, and welcome to Helios Technologies Second Quarter 2018 Financial Results. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. Should anybody require Operator assistance, please press star, zero on your telephone keypad.

It is now my pleasure to introduce your host, Miss Karen Howard, Investor Relations for Helios Technologies. Thank you. You may begin.

Karen Howard: Thank you, Jenn, and good morning everyone. We certainly appreciate your time today for our Second Quarter 2018 Financial Results conference call. On the line with me are Wolfgang Dangel, our President and Chief Executive Officer; and Tricia Fulton, our Chief Financial Officer. Wolfgang and Tricia will be reviewing the results that were published in the press release distributed after yesterday's market close. If you do not have that release, it's available on our website at www.heliostechnologies.com. You'll also find slides there that will accompany our discussions today. If you look through the slide deck, on Slide 2, you'll 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. These statements apply to future events that are subject to risks and uncertainties, as well as other factors that can cause actual results to differ materially from where we are today. These risks and uncertainties and other factors are provided in the earnings release, as well as other documents filed by the Company with the Securities and Exchange Commission. These documents can be found on our website or at www.sec.gov.

I also want to 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 to non-GAAP measures in a table that accompanies today's earnings release, as well as in the slides.

Wolfgang will get started with some highlights for the quarter, Tricia will go through the details of our financial results, and then we'll turn it back to Wolfgang for his perspective on our outlook, before we open up the line for questions and answers.

With that, it's now my pleasure to introduce Wolfgang.

Wolfgang Dangel: Thank you, Karen. Good morning, everyone.

I will start on Slide 3. Our team members around the globe have been working very diligently to advance our Vision 2025, within both our historic businesses, as well as our more recently acquired businesses.

Before I get into our results, I just want to highlight yesterday morning's announcement, that we have changed our corporate business name to Helios Technologies, in alignment with our Vision 2025. This is an important strategic step, as we are evolving. As we now have several operating companies under our umbrella, the holding structure provides the parent with an identity that is independent from our operating brands. It is important that the very well-known Sun Hydraulics name and strong brand will remain, but going forward, it will represent our cartridge valve technology business only. We will now use the Helios Technologies name when referring to the entire organization under the parent holding company. Our shares will continue to trade using the same ticker symbol, SNHY.

Now, let me give you an update on our business progress. This is the first quarter that will include the results of the Faster Group. To remind you, Faster is a global leader in quick-release couplers for hydraulic applications. As previously announced, we acquired this Northern Italy-based business on April 5th, just about the beginning of our second quarter. It carried a purchase price of about $533 million. We used proceeds from our February public offering to partially fund it, and we also amended our credit facility and used some of that new debt. The amended credit facility also gives us flexibility, as we continue to grow well into the future.

Our second quarter sales grew by nearly 52%, to more than $136 million, a record level for our Company. Of the $47 million in growth, about $39 million was contributed by Faster, and about $8 million was organic growth. The Faster business grew about 25% over last year's quarter, on a pro forma basis.

Regarding our organic businesses, we continue to experience very strong order demand in both Hydraulics and Electronics. In addition, we saw sequential improvements related to supply chain constraints compared with the past two quarters.

In our Electronics segment, we are now in a position to keep up with current order intake. In our legacy Hydraulics business, we have seen record order levels, and expect that shipments in the second half of the year will be stronger than the first half. This is reversing a historic pattern, as we work through the backlog and extended lead times created by the strong demand.

We have two major projects underway that will continue to increase throughput and capacity in 2019. Later this month, we will complete the relocation of our Korean business, from a smaller leased building into a newly constructed, state-of-the-art facility in Incheon, South Korea. This project will be completed ahead of schedule and within the original budgeted amount.

Additionally, we are well underway with optimization of the manufacturing footprint of our three Sarasota-based plants. We mentioned this project in last quarter’s call, and it is expected to be completed in early 2019. This project includes streamlining manufacturing processes and product flow in alignment with our Lean Philosophy. In addition, it will provide the platform to expand our engineering and R&D lab capabilities, which are scheduled to be finished by the end of 2019. The results of these efforts are concentrated manufacturing in two adjacent facilities, whereas R&D and engineering will be housed on a separate campus.

Overall, we were pleased with the operational improvements realized by our historic businesses during the quarter. We generated a 25.6% Adjusted EBITDA margin, up from 24% in Q1, and 20.5% in the fourth quarter of 2017.

Finally, as announced yesterday afternoon, we closed on the ‘bolt-on’ acquisition of Custom Fluidpower, based in Newcastle, in New South Wales, Australia.

Please turn to Slide 4, and I'll provide more details. Custom Fluidpower, or CFP is Australia's largest independent fluid power solutions distributor. As with most of our distribution channel partners, they are much more than simply a re-seller of product. They are very innovative, with a strong emphasis on delivering engineered solutions and value-add services from their eight branch locations across Australia. For the 12 months ended June 2018, they realized about $46 million USD of sales and a 9.7% EBITDA margin.

We really like the diversity of their customer base, ranging from mining and material handling to energy and oil & gas, as well as others, as shown here in the upper right box. Comprehensive value-add services they offer, are listed here in the lower left box. In addition to hydraulic manifold systems, they design circuitry, provide IOT (Internet of Things) and automation packages and even oversee broader turnkey projects. Additionally, there is an attractive aftermarket service component. We have featured one of their proprietary solutions in the lower right box – a custom brake power unit that includes some Sun products.

Please turn to Slide 5, and I'll talk about the strategic significance of this business to Helios. As you know, we believe it's very important to follow our business philosophy of 'in the region, for the region,' all around the globe. Custom Fluidpower gives us a strong physical presence in the Southeast Asia and Pacific region from which to build, especially given their engineering and design capability. We will leverage the in-roads that our Sun Hydraulics business has made into the region and we anticipate that CFP will accelerate our efforts.

Now turn to Slide 6, and I will summarize the transaction details. We just closed on this acquisition last week for a purchase price of about $26 million in a cash free, debt free transaction. The enterprise value amounts to about 5.6 times EBITDA on the trailing 12-month basis. It was funded as a 36% cash and 64% equity transaction. So we paid about $9.3 million of cash and issued $333,065 of SHNY shares. We have targeted approximately $2 million USD of EBITDA synergies by 2022, which will be driven by initiatives to increase sales in the region.

Regarding the financial impact to Helios, we expect that the acquisition will be EPS accretive in the first year, and that the transaction ROIC will exceed our cost of capital within a year. It is also worth noting that our net debt to trailing 12-months pro forma EBITDA is 2.6 after this transaction.

With that overview, I will now turn the call over to Tricia to review the financial results for the quarter and first half year in a bit more detail.

Tricia Fulton: Thank you, Wolfgang, and good morning everyone.

Let's begin on Slide 8 with a review of our second quarter consolidated results. Sales were up 52% compared with last year's quarter. Faster contributed 43% and our organic business sales grew 9%. Most of our products did not have any price increases, so nearly all of that growth is volume. Our Sun Hydraulics price increase was effective on July 1. So it will benefit our third and fourth quarters. Foreign currency translation had a favorable $400,000 impact for the quarter.

I will now touch on sales by region, which are designated here in the sales bar charts on the left. There's a table in the back of the press release, as well as the supplemental slides, summarizing this information. As you can see, all geographic markets realized considerable year-over-year growth. With the addition of Faster, the EMEA region is now a larger contributor to our sales base.

Sales to the Americas, EMEA, and APAC regions were 50%, 32% and 18% of the consolidated total, respectively.

Regarding profitability, our consolidated adjusted EBITDA was up 41% over last year's second quarter to $34.9 million or 25.6% of sales.

As we discussed last quarter, we continue to see margin pressure related to supply chain constraints and higher material costs. We anticipated that we would see these impacts in Q2 and to a lesser degree in Q3 and Q4. I'll get into this more as we review the segment results on upcoming slides.

Turning to the bottom line, adjusted earnings per share were $0.43 down 9% compared with last year's second quarter. This year's quarter includes $0.19 and $0.10 per share for amortization and interest expense, respectively, compared with $0.05 and $0.02 per share for amortization and interest expense, respectively, in last year's second quarter. Together, these two acquisition related items had a $0.22 impact on the second quarter comparison on both a GAAP and non-GAAP basis. Our GAAP and non-GAAP adjusted EPS for the 2018 second quarter also included a $0.05 charge for losses on foreign currency forward contracts related to the Faster acquisition.

I want to point out that our adjusted net income was up 7%, but our average shares outstanding increased due to our follow-on offering, impacting our earnings on a per share basis. I also want to highlight that our number of shares outstanding as of August 1, 2018 was about 31.9 million, given the shares issued to fund the Custom Fluidpower acquisition.

I'd like to bring to your attention the items that impacted our consolidated results and that we added back for purposes of reporting adjusted EBITDA and adjusted EPS shown here. Please refer to the tables in the back of the press release or slides for reconciliations of GAAP to non-GAAP numbers.

During the second quarter of 2018 we incurred the following:

- First, $3.1 million for amortization of inventory step-up costs resulting from purchase accounting for Faster.
- Next, we incurred $3.7 million of costs for acquiring and financing Faster and Custom Fluidpower.
- Next, we realize a $2 million charge on the foreign currency forward contract that we entered into when we signed the agreement to acquire Faster to lock in the Euro exchange rate.
- Finally, we recorded a $251,000 charge for contingent consideration associated with the Enovation Controls acquisition.

Please turn to Slide 9 for review of our second quarter Hydraulics segment operating results. Sales grew 70% to $103.6 million. We saw 41%, 144% and 46% year-over-year growth for the quarter in the Americas region, EMEA, and APAC. Those growth numbers benefited from the addition of Faster. On an organic basis, we realized growth of 6% and 21% in EMEA and APAC respectively, while sales to the Americas declined 1% due to supply chain constraints as well as a shift in customer delivery locations.

The regional allocation is impacted by a shift based on specific customer requests to have products delivered directly to their East Asian facilities, instead of delivery to their North American location. This inflates the APAC growth and decreases the Americas results for the quarter. This trend will continue into future quarters, making comparability a little more difficult, but highlights the global view we have of our business.

The organic growth was driven by our increased market penetration in new products as well as broad economic market expansion, partially offset by the impact of supply chain constraints and growing backlog. While gross profit increased by 54% on the higher sales including the addition of Faster, supply chain issues and material cost increases caused gross margin to decrease to 38%. We will reconcile that change in detail on the next slide.

Operating income increased 55%, realizing a reported operating margin of 24.5%. Our selling, engineering and administrative expenses or SEA, grew $4.8 million or 52% to $14 million compared with $9.2 million in the second quarter of the prior year. The increase includes $5.3 million for the Faster business offset by about $500,000 from cost reductions and efficiencies realized by the historical Sun business.

Please turn to Slide 10 and I will reconcile the change in gross profit from the second quarter of 2017 to the second quarter of 2018 for the Hydraulics segment. Gross profit in the 2017 second quarter was $25.6 million or 42.1% of sales.

- After adjusting for higher volume, we determined that we incurred about $1.5 million or 1.4 percentage points of margin for incremental material costs. This includes materials under long-term supplier agreements, as well as those not under agreement.

  As previously indicated, our Sun Hydraulics business implemented a price increase effective July 1. Given the timing of the increase at mid-year, we expect to realize approximately 1.5% to 2% additional net sales in Q3 and Q4 as a result.

- Higher production costs favorably impacted gross margin by about $200,000 or 0.2 percentage points of margin. This primarily consists of personnel-related costs resulting from inefficiencies caused by the supply chain constraints we've spoken about the past two quarters. With our new long-term supply contracts in place, we are pleased with the progress we've made and expect continued improvement in the third quarter.

- Next, we did realize favorable currency effect of about $300,000 or 0.3 percentage points of margin during the quarter, primarily due to the weaker U.S. dollar.

- Finally, Faster contributed $13.9 million of gross profit to the quarter, realizing a 35.9% gross margin on their $38.7 million of sales. The material costs, production inefficiencies, and offsetting foreign currency in total, impacted our 2018 second quarter gross margin by about 130 basis points. There were other normal fluctuations, such as varying sales incentives and mix that partially offset the leverage realized on the incremental sales. As we look into the third quarter, we expect further improvement and additional improvement in the fourth quarter.

Please turn to Slide 11 for a review of our Electronics segment operating results. Revenue for the second quarter grew 14% over the second quarter of last year. This was driven by ongoing increased demand in power controls and recreational vehicle end markets. In addition, proactive sales incentives and increased demand for our new products developed in the past year also contributed to growth.

Gross profit for the segment increased 8%, yielding a gross margin of 43.4% compared with 45.6% in the second quarter of 2017. I will reconcile that change in detail on the next slide.

Operating income in the second quarter grew 2% over the second quarter of 2017, with an operating margin of 20% in the 2018 quarter. SEA expenses grew $1 million, reflecting planned investments in selling and marketing initiatives as well as R&D to support our growth strategy, and accounting and administrative infrastructure costs, partially offset by cost savings from consolidating our HCT business into Enovation Controls.

Please turn to Slide 12 and I'll reconcile the change in gross profit from the second quarter of 2017, to the second quarter of 2018 for the Electronics segment. Gross profit in the 2017 second quarter was $13 million or 45.6% of sales.

- Similar to the Hydraulics segment, after adjusting for higher volume, we determined that we incurred about $600,000 or 1.8 percentage points of margin for higher material costs. The majority of these higher costs, approximately $400,000 were for excess and obsolete inventory. The remaining $200,000 was due to higher supplier costs.

- Production costs contributed favorably to the 2018 quarter compared with the 2017 quarter, by about $600,000 or 1.8 percentage points. This includes improved efficiencies and reallocation of application engineers from manufacturing overhead to our SEA reporting line.

- Finally, logistics also favorably contributed to the quarter by about $200,000 or 0.6 percentage points. Last year included inbound freight associated with stocking in the former San Antonio facility, prior to the completion of the carve-out.

- There were other normal fluctuations, such as mix and varying sales royalties that offset the leverage realized on the incremental sales. As we look forward to the third and fourth quarters, we expect further improvement.

Please turn to Slide 13 for a review of our first half consolidated results. Sales of $233.5 million were up 37% over last year's first half. Regarding profitability, our consolidated adjusted EBITDA grew 22%, resulting in 24.9% of sales in this year's first half. That was down from 27.9% last year.

Turning to the bottom line, adjusted earnings per share were $0.89, down from $0.90 last year.

Please turn to Slide 14 for a first half review of the Hydraulics segment. Sales of $166.2 million were up 45% over last year's first half. Gross profit increased by 32% on the higher sales, resulting in a 37.8% gross margin. That was down from 41.4% gross margin in last year's first half which I will reconcile on the next slide.

Operating income increased 29%, yielding a 23.3% operating margin, which was down from 26.2% operating margin in last year's first half.

Please turn to Slide 15, and I'll reconcile the change in gross profit from the first half of 2017 to the first half of 2018 for the Hydraulics segment.

Hydraulics gross profit in the 2017 first half was $47.6 million or 41.4% of sales.

After adjusting for higher volume, we've determined that increases in material costs were almost $2 million or 1.1 percentage points of margin. As you know, our July 1 price increase will start covering these cost increases in the third quarter.

Recall, we incurred interim labor costs in the first quarter. That cost was a premium we paid for experienced third-party contract labor that was isolated to the first quarter, again to try to keep up with demand and maintain our best in industry lead time. These amounted to about $500,000 in the first quarter of 2018 or 0.3 percentage points of margin for the first half. We discontinued the use of this type of labor, so these costs did not repeat in the second quarter.

We calculated that supply chain constraints, and resulting inefficiencies cost about $1 million or 0.6 percentage points of margin. This includes temporary labor and overtime, partially offset by process improvements.

Next, we had about $200,000 of extra logistics costs or 0.1 percentage points primarily outbound, but also some inbound freight costs. These were all incurred in the first quarter.

Finally, we did realize favorable currency effect of about $800,000 or 0.5 percentage points of margin, during the first half primarily due to the weaker U.S. dollar. The material costs, interim labor, production inefficiencies, logistics, and offsetting foreign currency in total impacted our 2018 first half gross margin by 160 basis points. There were other normal fluctuations, such as varying sales incentives and mix that offset the leverage realized on the incremental sales.

Please turn to Slide 16 for the first half review of the Electronics segment. Sales were up 20% over last year's first half. Gross profit increased by 11% on the higher sales, realizing a gross margin of 42.1%. That was down from 45.9% last year which I'll reconcile on the next slide.

Operating income increased 7%, yielding a 20.2% operating margin, compared to a 22.8% operating margin in last year's first half.

Please turn to Slide 17. Electronics gross profit in the 2017 first half was $25.6 million, or 45.9% of sales. Similar to the Hydraulics segment, after adjusting for higher volume, we determined that we incurred about $3 million of higher material costs, or 4.5 percentage points of margin. The majority of these higher costs, approximately $2.5 million, were incurred in the first quarter. Looking forward to the second half of the year, we expect supplier increases in ceramic components as well as tariff surcharges. We are actively negotiating with our key suppliers to secure stable pricing.

Finally, we calculated approximately $1.8 million, or 2.7 percentage points of margin, of favorable costs due to improved efficiencies, as last year we were in the midst of the carve-out process. There were other normal fluctuations, such as varying sales royalties and mix that offset the leverage realized on the incremental sales.

Please turn to Slide 18 for a review of our cash flow and capital structure. In the first half of 2018, we generated $31.1 million of cash from operating activities, compared to $21.7 million in 2017, with the 43% increase driven by higher net income and improved working capital, especially inventory. We finished the quarter with $29.9 million of cash, $355.2 million of debt, and $503.4 million of equity. The significant changes from year-end reflect our equity offering in Q1, and the Faster acquisition in Q2.

Subsequent to the end of the quarter, our acquisition of Custom Fluidpower used about $9.3 million in cash and increased our shares outstanding by about $333,000. We also made a $17 million payment for the earn-out of Enovation Controls during the first week of July.

Wolfgang, I'd like to turn it back to you for your perspective on outlook, and our updated guidance before we open the lines for Q and A.

Wolfgang Dangel: Thanks, Tricia. Please turn to Slide 20. The leading indicators that are important to Helios continue to see more ongoing growth through the rest of 2018. However, the rate of growth in the U.S. and all major global economies is expected to be at a slower pace of growth in late 2018. Leading indicators point to a mild recession in the next 12 to 24 months. Important to note, we have stated that in accordance with our Vision 2025 plan, we expect to outpace macroeconomic growth. This is being driven by the investments we have been making to expand our coverage in the field, increase and broaden relationship with OEMs, penetrate regions where we have white space, and continue to introduce new and innovative products and solutions.

Separately, we are cognizant of the potential impact of the changes related to tariffs. We have begun to notify customers, that if there is a negative tariff impact, we will pass it on in the form of a corresponding surcharge.

Please turn to Slide 21 for thoughts regarding our outlook for Helios. Regarding our organic businesses, strong demand and our backlog give us confidence in our growth expectations for the remainder of the year. From a profitability standpoint, while certain cost pressures will continue into the third quarter, as Tricia mentioned, they are declining as a result of actions we have taken. Further, our Sun price increase, which is the first in three years, is taking effect in the quarter we are currently in, and we expect that it will offset the manufacturing cost inflation we have been burdened with over the past couple of quarters.

I want to remind you that our investments in our SEA initiatives are necessary and will continue, as we are driving top line growth in accordance with our strategy and providing support for our growing organization.

Finally, may I point out that our historic Sun and Enovation Controls businesses are seasonally weakest in the fourth quarter. However, we don't expect this to be the case this year for our Sun business, given the demand we have seen from the marketplace and our strong backlog.

Regarding Faster, we have included this business in our 2018 guidance beginning April 5th, when we closed on the acquisition. Faster experienced 25% growth in the second quarter of 2018 over the prior year quarter. Their historical pattern is that the first half of the year is stronger than the second half by a ratio of about 53 to 47. We continue to anticipate this will likely be the case in 2018.

Please proceed to Slide 22 where we updated our guidance for 2018. Compared with the guidance we've provided in May, we are now including Custom Fluidpower for the last five months of the year in our Hydraulics segment, so we are expecting revenue between $510 million to $525 million on a consolidated basis. This amounts to consolidated organic revenue growth of 12% to 15%, unchanged from last quarter. We expect that revenue for our organic Hydraulics business will grow between 13% and 15%, and revenue for our Electronics business will grow between 9% and 13%.

We revisited our consolidated adjusted operating margin guidance and lowered our guidance by one percentage point to 21.7% to 23% following our current reporting methodology, which excludes acquisition-related amortization of inventory step-up and intangibles, as well as other one-time type costs.

Our effective tax rate, capital expenditures, depreciation and amortization guidance have all been updated to include Custom Fluidpower and the impact of purchase accounting based on our latest estimates.

Before we open up the lines for questions and answers, I want to make you aware that we have scheduled an Investor and Analyst Day for later this year. It will be held on Wednesday October 3, in New York City. If you are available to attend, please contact Kei Advisors, our investor relations firm, at the contact information provided within our earnings release.

Now let's open the lines for Q&A.

Operator: Thank you. Ladies and gentlemen, it's time for a question-and answer-session. You may ask a question anytime via the webcast, or to ask a question by phone, please press star, one on your telephone keypad. A confirmation tone will indicate your line in the question queue. You may press star, two if you would like to remove your question from the queue. For participants using speaker equipment, it may be necessary to pick up the handset before pressing the star key. One moment please, while we pull for questions.

Our first question comes from the line of Jeff Hammond with KeyBanc Capital Markets. Please proceed with your question.

Jeff Hammond: Hey, good morning.

Tricia Fulton: Morning.

Jeff Hammond: Really just want to dig into the Hydraulics supply chain constraints. How much do you think that held back sales in the quarter? What’s changing in the facilities to help alleviate those supply chain constraints into the second half?

Wolfgang Dangel: Yes. Let me answer the second part of the question first, Jeff. As we said already on the previous call and as we reiterated today, we are going through consolidation efforts here in terms of streamlining manufacturing, where we are bringing manufacturing from three campuses to two basically adjacent facilities here in Sarasota. By doing so, we are freeing up the third facility pretty much for the engineering and R&D center that we want to invest in over the next couple of years.

So, as I pointed out earlier on, through streamlining the initiatives here on the manufacturing side, that will free up additional capacity and will shorten throughput. We can pretty much convert that additional capacity into output for next year. We are going through that project that is going to be completed by the beginning of the first quarter of 2019.

Jeff Hammond: Okay. Then just on the price increase, how quickly and firmly do you think you can push this through into the second half? It just seems like material costs are weighing on the margin. I just want to get a better sense of how quickly you'll alleviate that.

Wolfgang Dangel: Yes. So the price increase, Jeff that went into effect July 1st. I mean, we gave notification to channel partners and customers already six weeks in advance, so during the course of the second quarter already. We have rolled that out. We are basically calculating on a 1.5% to 2% net impact on sales for the balance of the year. Everything we are seeing and observing so far, is going reasonably smooth. Probably the 1.5% to 2%, it might even be a little bit of a conservative assumption.

Jeff Hammond: Okay. Just back on the supply chain. I think in the bridge, you showed productivity is slightly positive in Hydraulics. Is there an offsetting supply chain headwind there that's holding back productivity? Then as we look into the second half and you pick up some of the supply chain, that's a bigger tailwind?

Tricia Fulton: The production costs in the Q2 Bridge for Hydraulics is actually a slight downside of $200,000. Is that the number you're referring to?

Jeff Hammond: Yes. I guess I was looking at the second quarter number which was I think slightly high.

Wolfgang Dangel: On Slide 10, production is slightly down, 0.2%.

Jeff Hammond: Slightly down, okay. Yes. Does that number turn positive as the supply chain constraints get alleviated?

Wolfgang Dangel: Yes. That's the assumption, Jeff. That number will turn positive.

Jeff Hammond: Okay.

Wolfgang Dangel: There is already a significant improvement over prior quarters. You might recall when we reported that on the bridges during the previous call. So that is depleting over time and is expected to turn positive then.

Jeff Hammond: Okay. Then just on interest, what's driving the much higher interest expense versus just last quarter?

Tricia Fulton: Yes. LIBOR has gone up faster than what we had planned in our previous guidance. We have taken on a little bit more debt as well related to the Custom Fluidpower acquisition. We have very recently entered into some swaps to fix part of the interest rate on the debt. Initially upfront, you pay a little bit more, but we believe longer term it's the right decision to fix those rates with the swaps.

Jeff Hammond: With the swaps, what's the fixed/floating mix now?

Tricia Fulton: It's about half and half right now.

Jeff Hammond: Okay, great. Thanks guys.

Tricia Fulton: Thank you.

Operator: Thank you. Our next question comes from the line of Charley Brady with SunTrust Robinson Humphrey. Please proceed with your question.

Charley Brady: Thanks. Good morning. Just on that last question on the fixed/floating, what's the rate that you're fixing?

Tricia Fulton: The grid is LIBOR plus whatever tranche we're in. We're at 2% plus LIBOR and that fixed LIBOR is about 2.8% for five years.

Charley Brady: Thanks. Five years. Okay. Just want to clarify on the price increases that went in effect, July 1, going into Q3, does that put you price/cost neutral, so there is not a material headwind in Q3? Or does that have to take to Q4 to get there?

Tricia Fulton: It'll take until Q4 to get there. We do have some backlog that is still priced at the old pricing, that needs to flow through and that's going to flow through, hopefully the majority of it, in Q3. We don't get the full impact of the price increase right away because of that. I think we even said last quarter that we expect that the price increase will cover material costs for the entire year. So, it will take us through the end of the year to realize that uptick.

Charley Brady: I just want to clarify that point. If you're saying it's going to carry it for the full year, does that mean, you've been negative headwind here a couple quarters on the first half of the year, are you saying that for the full year all in, you're going to be neutral so that you actually make up everything that was a negative in the first half and part of Q3 as well?

Tricia Fulton: Yes. That's correct.

Charley Brady: I didn't understand your explanation on the Electronics piece, on the production. There was something moving from that to a Selling, Engineering & Administrative category. Can you just repeat and clarify what you said about that?

Tricia Fulton: Yes, part of the increased production that you see in that bridge, is a pickup for the gross profit that is related to a shift of people out of manufacturing overhead and into SE&A, as a bit of a restructuring of that business. So, the costs don't go away they just shift into the SEA line; that already happened for the majority of Q2.

Charley Brady: Okay. On the price increase, you said you communicated it about six weeks ago to customers. Do you think that's had any pre-buying effect that might have pulled sales from the second half into the second quarter?

Wolfgang Dangel: Yes, so just to clarify. We communicated about six weeks prior to the date of effectiveness. So, we communicated about mid of Q2. To answer your question, yes, I assume probably that it elevated order rates a little bit, but I don't think it is substantial or material because we clearly see that the marketplace is really demand driven, and hardware is being deployed in applications around the world as quickly as it gets available.

Charley Brady: Thank you.

Operator: Thank you. Our next question comes from the line of Mig Dobre with Robert W. Baird. Please proceed with your question.

Mig Dobre: Yes, good morning everyone. First, if I may, just a clarification on guidance. I understand the revenue has reflected Custom Fluidpower. Can you give us a sense as to what some of the other changes were? Core and also due to Custom Fluidpower?

Tricia Fulton: Yes, so we see that increase in Hydraulics revenue that reflects what we believe the last five months of Custom Fluidpower's revenue will be. We also made an adjustment to line items for amortization, depreciation and interest on the additional debt that we pulled related to that. Additionally, we did adjust operating margins down about a percent, and a part of that is related to the fact that we're bringing in Custom Fluidpower into the fold, and their operating margins are a bit lower than what the traditional Helios businesses are running at. The remainder of that decrease is related to some of the challenges that we're seeing on the gross profit side related to supply chain constraints and inefficiencies.

Mig Dobre: Right. So, of the 100-basis point trade, what would you estimate is challenges with margin versus Custom Fluidpower itself?

Tricia Fulton: Yes, about 40% of it is Custom Fluidpower and 60% of it is challenges the traditional businesses are seeing.

Mig Dobre: Okay. Then, on the depreciation and amortization, the increases of $2 million on each of those lines are related to the Custom Fluidpower acquisition?

Tricia Fulton: Yes.

Mig Dobre: Okay. Am I to assume here that on the $20 million of revenue from Custom Fluidpower, there is a $2 million EBITDA contribution given with the margins they're running?

Tricia Fulton: Yes, that's fair.

Mig Dobre: Okay. I'm struggling to see exactly how this is going to be accretive then if we're talking about incremental D&A, as you talked about it, of $2 million and $2 million, but I guess I'm going to take this off line to run through the numbers.

Tricia Fulton: Yes. It's not a full $2 million tick on both the amortization and depreciation. I think there were some adjustments also related to the purchase accounting for Faster, especially on the amortization side and some adjustments to depreciation for the traditional business given some of the capital that's coming on board.

Mig Dobre: Okay, I see. Then, maybe switching to the base business in the quarter. You know, when I'm looking at these gross margin bridges that you provide on Slide 12 and Slide 10, which they're really helpful, so thank you for those. If I'm excluding the material cost, production, currency, acquisitions, logistics, all these items and I'm just looking at the sales, volume and mix impact. It looks to me like the incremental margin, gross margin, in both Hydraulics and Electronics was quite weak. It was something like 32% in Hydraulics, 22% in Electronics, a pretty material step down from last quarter. So, I'm scratching my head trying to figure out exactly what happened here and what gives you the visibility and the expectation that in the back half we're going to see better pull through on this particular item, sales, volume and mix.

On Slide 10, I'm talking about the 1.3 contribution from sales, volume and mix. As I understand this, you're basically saying that on the core volume that you've delivered year-over-year, this contributed $1.3 million to gross profit, right?

Wolfgang Dangel: Right.

Tricia Fulton: Yes.

Mig Dobre: Right. So, if that's the case then what we're talking about here is there is an implied incremental gross margin of 30 something percent about 32.5%. Last quarter, using the same math, you did something like 43%. So, it's either that the mix, maybe the mix is different and maybe there's something else that is going on here from one quarter to another. But the point is, that even if your pricing comes through in the back half and offsets your material cost at 1.4% headwind, the core business has to improve significantly. I'm wondering, again, how do we get there and what happened in the quarter?

Tricia Fulton: So, in looking at the volume and the mix, it was offset by sales incentives. As you recall the historic Sun business has always had a large expedite premium. Obviously, with our backlog in past due, we are not recognizing that expedite premium in the current quarters. We also have a decrease in average sales price because of the volume of purchases. We have volume discounts, so as volumes go up, the discount becomes higher, as well as some of our regional allocation of sales which sometimes have different margin profiles as well. So, those sales incentives pulled off at least $1 million in Q2.

Mig Dobre: Okay. Do you have any price increases planned for Electronics or was that comment only for Hydraulics?

Tricia Fulton: That comment was only for Hydraulics. The Electronics business had a price increase at the beginning of the year for the portion of the business that's primarily related to distribution sales. They have a high amount of OEM sales, so price increases are set by the contract with the OEMs directly. We have not been able to affect pricing changes this year in the Electronics business other than the small price increase that went to distribution at the beginning of the year.

Wolfgang Dangel: As we pointed out last time, Mig, the opportunity for pricing changes is with release changes or with new projects coming, as we talked about it on the last call.

Mig Dobre: Right. Two more for me. So, going back to your comments vis-a-vis the backlog in Hydraulics, can you give us a sense here for the magnitude of what we're talking about here? Maybe dollar magnitude or however you want to frame it, in order to get a little more comfortable with the growth rates on top of comps in the back half?

Wolfgang Dangel: Yes, we don't want to go into specific backlog or order dollar numbers, but I can tell you that we are seeing order intake at record levels as we have never seen in the past, and even if we do the comparison to our peer group, we see clearly elevated order levels here. That's the main reason why the back half, the second half of the year is stronger than the first half. Whereas, this was different in the past as you know very well Mig.

Mig Dobre: Okay. Then, maybe last question on the Custom Fluidpower acquisition. So, I'm trying to understand that business a little bit better. How much of what Custom Fluidpower does is some of these value-add services that you mentioned versus just pure distribution revenue, and is there any channel conflict that might be created here? What does it mean for any of the other relationships that Custom Fluidpower has with other OEMs? How should we think about that?

Wolfgang Dangel: Yes, so first of all the majority of the business is value add, project based driven, value add engineered business. There is also a proportion of component sales but the vast majority is engineering driven businesses. To the second question, the business there is spread out over many, many manufacturers there and there is no conflict with any other supplier. In this case, we did a thorough analysis during the due diligence process. That's all, that's okay.

Mig Dobre: All right. Thanks for taking my question.

Tricia Fulton: Thank you.

Operator: Thank you. Our next question comes from the line of Brian Drab with William Blair. Please proceed with your question.

Joe Aiken: Thanks. This is actually Joe anchoring for Brian this morning. I was wondering if you could talk a little bit more about one of your growth opportunities, which has been to penetrate geographies where you've historically been weaker. I know you touched on the increased demand and all, and markets on the slide. I was wondering if you could talk a little bit about the gains you've made with this initiative in 2018.

Wolfgang Dangel: Yes, sure. I mean, we had started about two years ago focusing on some of those geographies. We refer to them as 'white spots.' Those are historically areas where we hardly had any revenue. In this particular case, we are aiming to leverage the position we have with Custom Fluidpower in Australia and try to enter into the Southeast Asian marketplace. Just to give you a practical example, in Southeast Asia, until three years ago, I think we had one single distributor in the entire region. So what we did over the last two years, 18 months, we added four distributors and three integrators. So, in the meantime we have about 10 channel partners across Southeast Asia. It is mainly Thailand, the Philippines, Indonesia, Vietnam, these countries that are neighboring Australia so to say.

What we are trying to do on one hand, we're signing up channel partners. We will also put some of our boots on the ground there. Then of course it will be heavily supported out of Australia because this is where we now have the engineering capabilities, across those eight offices scattered across Australia. If you look at Custom Fluidpower, their largest office is actually in Mackay, that's in the northern territory, in North Queensland, of Australia. That's closer to Indonesia than it is to Sydney. With their capabilities, they can then help us to better penetrate the Southeast Asian market.

You asked in general, if I understand your question correctly, about these types of markets or geographies. We're trying two additional things in other geographies as well as in India where we have a presence already, but we are still adding people. We are signing up channel partners there. So, we want to have a better penetration of the Indian market as well. These types of emerging markets where a lot of machine building and equipment manufacturing is taking place now, we want to make sure that we are well positioned in those geographies. Does that answer your question?

Joe Aiken: Yes. Thanks for the color there; that was very helpful. Then just a quick follow up. How is your backlog in each of the businesses, Hydraulics and Electronics? How is the backlog compared with this time last year?

Wolfgang Dangel: Faster, I'm not 100% sure, but backlog also has gone up at least since we did the due diligence in the fourth quarter of last year. CVT (cartridge valve technology), our Sun core business, has gone up considerably because of the high order intake that we have been seeing particularly over the last nine months. In Electronics, it's gone slightly up, but not significantly higher than about a year ago.

Joe Aiken: Okay, great. That's helpful. Thanks for taking my questions.

Operator: Thank you. Our next question comes from the line of Adam Farley with Stifel. Please proceed with your question.

Adam Farley: Hey, good morning. Thanks for taking my questions.

Tricia Fulton: Good morning.

Adam Farley: I want to follow back up on the sales incentive question for Hydraulics orders. Were there any charges or liquidated damages on past due orders, or do you expect to see anything there, or is it just delayed orders?

Wolfgang Dangel: That's the way it fell in place. So, there is none and we're not expecting anything for the future.

Adam Farley: Perfect. Then, shifting gears to Electronics, I saw the press release called out sales initiatives and new products driving part of the growth. What type of new technology offerings and products are you guys having success with?

Wolfgang Dangel: That's still in line with pretty much the successes that we have seen last year. I mean, we're launching about 10 new products every single year now. The last two years back in 2017, and another roughly 10 in 2018 here as well. It's still the same modus operandi at the end of the day. I mean, we're deeply embedded within the engineering skills of the OEMs, particularly in those growth markets, marine to name one, and this is where we see most of those successes. We continue to heavily invest into R&D, to launch more products as we move forward from here. We feel pretty strongly that we have a winning formula in place with the way we go after business. We will maintain doing exactly the same thing that we have been doing over the last 20 months here.

Adam Farley: All right. Great. Thank you.

Operator: Our next question comes from the line of Jon Braatz with Kansas City Capital. Please proceed with your question.

Jon Braatz: Morning, Wolfgang and Tricia.

Tricia Fulton: Morning Jon.

Jon Braatz: Wolfgang, you made a comment about tariffs. I'm wondering if you're hearing anything from your customers about tariffs whether they're being helped on the sales level, being helped or hurt by all this tariff talk.

Wolfgang Dangel: If you can imagine, Jon, there is a lot of disarray, I would say, in the marketplace right now. So, we've been analyzing the situation rather thoroughly over the last three, four weeks, since July 6, actually since the major announcements have been coming out. Yes, to answer the question. We are hearing from customers, from OEMs, and also from channel partners who are dealing with end customers and OEMs. The message I think is mixed at this stage. There are circumstances where OEMs are understanding and will accept it. I think there are circumstances where people will also push back. So every case here is a little bit different. It's a highly complex topic where today nobody has clear transparency to be quite honest.

Jon Braatz: Okay.

Wolfgang Dangel: Our assumption is that we notified our customer base. If we don't directly import anything that falls under the tariff, but if we're ending up here with cost increases, we would have to pass it on. So we notified the customer base.

Jon Braatz: Sure. Okay. Tricia, on your amortization guidance of about $23 million, you had $10 million for the first half including $8 million in the second quarter alone. If I would extend that $8 million per quarter in the second half, it would be a little bit higher than that $23 million. Were there some one-time amortization charges in the second quarter that won't continue?

Tricia Fulton: Yes. There was some one-time Faster amortization related to backlog that came off relatively quickly.

Jon Braatz: Okay. All right. On what line item did you include the $3.7 million acquisition costs and finance costs?

Tricia Fulton: That would have been in SEA.

Jon Braatz: All in SEA?

Tricia Fulton: Yes.

Jon Braatz: Okay. All right. Then looking ahead into the second half, do you anticipate any additional one-time transaction costs or financing costs or anything like that in the back half of the year?

Tricia Fulton: We do still have some step-up for inventory related to the Faster acquisition that will take place in Q3, about $2 million, that will hit in the cost of materials line, our gross margin. Other than that, there's not a lot that we're anticipating. We will have some costs in the third quarter related to the acquisition of CFP, but it won't be to the degree of the cost that we saw with Faster's since it was a smaller acquisition.

Jon Braatz: Right. Okay. All right. Thank you Tricia.

Tricia Fulton: Thank you.

Operator: Thank you. Ladies and gentlemen, this concludes today's question-and-answer session. I would like to turn the floor back to the management for any closing comments.

Wolfgang Dangel: Thank you very much for your interest in Helios and for your participation this morning. Also, thank you to all of the hardworking Helios employees who are driving these results. Welcome to our Custom Fluidpower employees. We look forward to updating all of you on our third quarter results in November. Thank you very much and have a great day.

Operator: Thank you. Ladies and gentlemen this concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation.