Tania Almond

Thank you, operator, and good day everyone. Welcome to the Helios Technologies First 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 Tricia Fulton, our Executive Vice President, and Chief Financial Officer. They will spend the next several minutes reviewing our first quarter results, discussing our progress with our augmented strategy, reiterating our outlook for 2023, 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 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 and 4** now.

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

Josef Matosevic

Tania, thank you, and thanks to everyone on the line joining us.

The vision we have laid out is really starting to come together. The Helios team continues to execute on our Augmented Strategy. THANK YOU to all the Helios colleagues for your tireless work and critical contributions in executing our shared vision.

We started 2023 with strong top-line results. Our team delivered very good sequential revenue growth of 9%, including double digits from electronics, coming off the fourth quarter. We are encouraged, by the continued improvement we have seen in our health and wellness business over the last few months.

We are protecting the business by achieving a sequential increase on our gross margin, while navigating the macro environment, supply chain, and FX impacts.

We are proactively investing through operating expenses over the first half of this year. This will accelerate the integration of our augmented strategy to align our long-term cost structure as we continue this journey and prepare for the next wave of global growth. We view these investments as more of a step function in how it will play out through our financials. There are several investment areas…

First, following the acquisition and integration of several companies, we announced the opening of two new Centers of Excellence to be completed in Q3. This is part of the construction we are highlighting on slide 4 currently taking place at Daman adding 50,000 square feet. We just turned the lights on and took down the temporary wall between the addition and existing building. We are also starting construction right next to our existing Balboa facility in Mexico to add 68,000 square feet.

Second, we continue to do the work we previously outlined relating to our manufacturing and operating roadmap projects. We have several initiatives we will execute throughout 2023 and beyond, that will drive efficiencies and improvements across the business. An example of this is moving targeted board assembly and wire harness production from Tulsa to Tijuana. In fact, as we have been implementing these actions to increase capacity, new customer opportunities have been created mid-stream that we are responding and adjusting to.

Third, we are happy to announce that we are moving to a regional organizational structure for our Hydraulics segment. After reaching a critical mass from the addition of several flywheel acquisitions, the time has come to adjust our structure to position us for the next wave of growth. A lot of time and planning has been invested to make this happen.

For our new regional structure, Matteo Arduini our long-time President of QRC will have full oversight for Hydraulics in EMEA. Rick Martich, who has been our longstanding head of manufacturing and operations, was just promoted to President of Hydraulics for the Americas. In December, Lee Wichlacz joined Helios as the President of the Electronics segment. Matteo, Rick, and Lee will work together to support our customers in APAC with our local leadership team in that region. We now have our updated structure in place that brings strong leadership, knowledge of our brands and customers, great team chemistry, and leaders who work extremely well together.

We expect this new regional structure, the company's Centers of Excellence, and our manufacturing and operating strategy, to support growth well beyond our $1 billion total company milestone. We believe the time is right to make these important investments which will have a short-term impact on our operating margins. We are executing to our full year outlook with our manufacturing and operating strategy driving productivity and efficiencies, protecting full year margin and earnings while navigating a challenging operating environment.

Now turning to **Slide 5**. Last week we announced a definitive Agreement to acquire i3 Product Development. i3 has over 55 engineers with expertise in electronics, mechanical, industrial, embedded and software engineering. They will further diversify our end markets through their experience across medical, off-highway, recreational and commercial marine, power sports, health and wellness, ag, consumer goods, industrial, and sports and fitness.

Innovation is the lifeblood of any successful organization. We expect the acquisition of i3 to turbocharge our efforts to be the most innovative company focused on the intersection of hydraulics and electronics.

They will equip Helios with significant value-added professional service capabilities to solve customers' most complex needs and provide customization for Helios platforms and solutions. Their patented remote platform will provide support in the field for customers and their IoT devices. Over their 28-year history, i3 made a pivot in 2017 to broaden their focus to include cloud, connectivity, IoT and electronics. Since that time, their growth has really taken off. It will be a powerful combination to apply their capabilities and expertise against the scale of the global Helios business as we approach $1 billion in annualized revenues.

i3 fits perfectly into the telematics and data analytics roadmap we have been articulating for quite some time. Their culture is very aligned with ours. It is a rare opportunity to find a company of this caliber that provides top notch engineering and software capabilities that will plug perfectly into our own roadmap vision. We are very pleased to welcome them to the Helios family.

Now let me turn the call over to Tricia to review the financial results and reiterate our outlook. She will then hand it back to me for a few final comments. Tricia, please.

Tricia Fulton:

Thank you, Josef and hello, everyone. On **Slide 6 through 10**, I will review our first quarter 2023 consolidated results.

We saw strong sequential improvements coming off the fourth quarter. We had sequential growth on revenue, gross margin, and adjusted EBITDA while investing in our future. This gives us increasing confidence in how we see the rest of the year unfolding relative to our original expectations.

Industrial and mobile markets realized double-digit percentage growth in the quarter over the year ago period. Within these markets, there was growth in machinery, construction, material handling, specialty vehicles, power generation, oil and gas, forestry, and renewable energy. Agriculture demonstrated single digit annual growth while our health and wellness markets remained contracted compared to the year ago period but grew 36% sequentially.

Our strong revenue growth over Q4 22 of 9% was driven by the Electronics segment which was up 17% with the Hydraulics segment up 5%.

Year over year, Hydraulics was up 8% (or 10% in constant currency) and Electronics up 11% (excluding Health and Wellness) over Q1 22.

Geographically, we saw growth across all regions sequentially, led by EMEA with 15% growth, the Americas at 8% and APAC at 4%. Over the year-ago period, revenues declined in all regions reflecting lower demand primarily in the health and wellness market. Overall, we had an unfavorable FX impact on revenue of $3.5 million in the quarter compared with first quarter 2022. Most of the FX impacts affect the Hydraulics segment.

Sequentially, gross profit grew 12% and gross margin increased 110 basis points over the fourth quarter driven by higher volumes. As we would expect, on a year-over-year basis the lower volumes impacted our gross profit. Gross margin compared with last year was impacted by reduced leverage of our fixed cost base on lower sales and the margin profile of acquisitions, which were partially offset by favorable sales mix and the impact of price increases.

Our SEA expenses increased 9% sequentially to $38.1 million. As Josef outlined, we are making several important investments at this time which drove that increase. Sequentially, Adjusted EBITDA increased 10% and Adjusted EBITDA margin was up 30 basis points over the fourth quarter levels. We continue to demonstrate we can provide top tier margins through a challenging macro environment. We achieved this while investing in our future structure to leverage the multiplier effect of integrating our flywheel acquisitions.

Our effective tax rate in the first quarter was 22.8% compared with 22.4% in the prior-year period reflecting levels of income in domestic versus international tax jurisdictions. Diluted non-GAAP cash EPS of $0.72 in the quarter reflects higher interest expenses compared with last year of 6 cents and a 4 cent impact for FX.

Slides 9 and 10 provide visual trends on overall key metrics for the past several quarters. We estimate that supply chain constraints delayed $12.4 million in sales this quarter, relatively flat sequentially and down from $17.6 million in the year-ago period. The coil shortage we discussed last quarter in Hydraulics has slightly improved. However, this quarter we experienced part shortages as well as some out-plant processing delays.

This quarter revealed an inflection point in our Electronics segment, with absolute revenue dollars growing sequentially for the first time since Q1 22. As you know the softness we experienced in the health and wellness market coming off the boom cycle in 2021 was the driver of that decline. We remain cautiously optimistic this can become a sustainable trend throughout the rest of the year. As we said last quarter, we believe the health and wellness market may have bottomed out and we are starting to see the signs of a recovery in our 2023 results.

On **Slide 11**, you will find the highlights for our first quarter Hydraulics segment. Sales grew 10% on a constant currency basis over the prior year period and the unfavorable FX impact was $3.3 million. Acquisitions added $13.7 million. Sequentially, this segment grew 5% over Q4 22.

The Hydraulics segment's gross profit increased $1.4 million, or 3%, sequentially over Q4 22. Compared with the prior-year period compression in profit dollars was primarily due to material price increases, unfavorable FX of $0.8 million, and restructuring costs of $0.7 million. The gross margin this quarter compared with Q1 22 reflects higher material and energy costs, for which margin was not fully recovered by pricing efforts, as well as the different margin profile of our recent acquisitions.

SEA expenses increased by $2.8 million, or 15%, year over year, and increased 90 basis points to 14.9% of sales. The increases were driven by acquisitions as well as the investments we outlined related to the company's strategy.

Please turn to **Slide 12** for a review of our Electronics segment. This segment is more concentrated in the U.S., so foreign currency had only a minor impact of $0.2 million on revenue for the quarter.

Electronics Sales decreased over the prior year period by 37% to $65.5 million, with demand across all regions declining as mentioned, due primarily to the contraction of the health and wellness market. When excluding the health and wellness market, the Electronics segment grew 11% over Q1 22. End market demand was driven by industrial and mobile markets. Sequentially, as mentioned, we saw very strong growth in this segment.

The Electronics segment's gross profit of $21 million grew 44% sequentially over Q4 22 with gross margin expanding 590 basis points. Year over year, the gross profit dollars reflect the slowdown in the health and wellness market. The gross margin increased 40 basis points over the Q1 22 level driven by a favorable sales mix.

SEA expenses were managed and declined sequentially 3% over the Q4 22 level.

Please turn to **Slide 13** for a review of our cash flow. We had solid cash flow generation. In Q1, we generated $12.3 million in cash from operations. Cash and cash equivalents totaled $36.3 million, up 10% over the year ago period.

CapEx came in at 4% of sales for the quarter, in line with our expectations to support our strategic investments for future growth, as Josef outlined on slide 4. And we recently paid our 105th sequential quarterly cash dividend.

Free cash flow was $72.1 million on a trailing twelve-month basis with a conversion rate of 88% compared with 79% for the full year 2022.

You can see on **Slide 14** that we have a solid balance sheet and financial flexibility to execute our strategy for growth. Total liquidity at the end of the quarter was $91 million. Our net debt to adjusted EBITDA leverage ratio was 2.5x reflecting the acquisition of Schultes. We estimate pro forma for our recently announced i3 flywheel acquisition, our net debt to adjusted EBITDA leverage ratio will be ~2.6x. As a part of that transaction, a good portion of the deal consideration will be paid in Helios equity to align the talented engineering resources with the long-term success of our combined strategy.

As you know, we have a well-established track record of managing our leverage ratio as we execute on our acquisition strategy. As we increase above our target level for recent acquisitions, we have been able to quickly de-lever back to or below our target leverage ratio of 2 times based on our cash generation.

Turning to our 2023 outlook, please reference **Slides 15 to 17**. We are re-iterating our outlook of growing revenues to between $910 million to $940 million this year. That would imply 3% to 6% annual growth over 2022 and over 20% growth compounded over the last three years since 2020. We continue to expect to be able to reach our $1 billion revenue milestone with top-tier margins on a run-rate basis ending the fourth quarter of 2023.

Based on our strong sequential revenue growth in the first quarter, we now estimate our first half to second half revenue split to approximate 47% to 53% respectively. With the timing of the investments, we outlined and the higher revenues in the back half of the year, we expect approximately a 100 to 250 basis point sequential improvement on EBITDA margins as we work toward our year-end run-rate target.

Importantly, we still see a path to deliver our original target set at our last Investor Day to achieve a three-year CAGR of approximately 22% growth in non-GAAP cash EPS, at the midpoint of our expected range for 2023 of $3.95 to $4.10 per share.

I would like to hand it back over to Josef for some closing comments before we take your questions.

Josef Matosevic:

Thank you so much, Tricia. We are off to a solid start in 2023. We continue to build on the strong foundation we established over the last few years, by executing the **augmented strategy** we laid out. We remain focused on being an industry leader in innovation and providing our customers the attention and dedication they have come to expect.

We continue to acquire high-quality portfolio flywheel acquisitions that **advance our technologies** with industry-leading products and solutions. We are making significant progress implementing our manufacturing and operating strategy as we diversify revenues and markets while protecting our business and margins, all which has **accelerated our growth**.

So, as we progress into 2023, our vision and goals remain unchanged.

We believe we can protect the business, cash flow and earnings, and that the Helios business system will continue to provide the structure and discipline to execute our long-term plans.

Through our organic and acquired innovations, we have created a pure-play hydraulics and electronics business that will continue to drive shareholder value well into the future.

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