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TTM Technologies, Inc. (TTMI) Q3 2022 Earnings Call Transcript

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Q3: 2022-11-02 Earnings Summary

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EPS of $0.56 beats by $0.13 | Revenue of $671.08M (20.53% Y/Y) misses by $4.43M

TTM Technologies, Inc. (NASDAQ:TTMI) Q3 2022 Earnings Conference Call November 2, 2022 4:30 PM ET

Company Participants

Sameer Desai - Senior Director, Corporate Development & IR

Thomas Edman - President and CEO

Todd Schull - EVP and CFO

Conference Call Participants

William Stein - Truist Securities

Michael Crawford - B. Riley Securities

James Ricchiuti - Needham & Company

Tyler Burmeister - Craig Hallum

Matthew Sheerin - Stifel

Sameer Desai

Thanks for everyone's patience. So we're going to start the call now. I've got Tom Edman with me and Todd Schull as well. So let me just read the safe harbor statement before we get started. So before we get started, I want to remind everyone that today's call state forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995, including statements related to TTM's future business outlook.

Actual results could differ materially from these forward-looking statements due to one or more risks and uncertainties, including the factors explained in our more recent annual report on Form 10-K and other filings with the Securities and Exchange Commission. These forward-looking statements are based on management's expectations and assumptions as of the date of this presentation. TTM does not undertake any obligation to publicly update or revise any of these statements, whether as a result of new information, future events or other circumstances, except as required by law.

Please refer to disclosures regarding the risks that may affect TTM, which may be found in the other reports on Forms 10-K, 10-Q, 8-K, the registration statement on Form S-4 and the other company's SEC filings. We will also discuss on this call certain non-GAAP financial measures such as adjusted EBITDA. Such measures should not be considered as a substitute for measures prepared and presented in accordance with GAAP, and we will direct you to the reconciliation of non-GAAP to GAAP measures included in the company's press release, which was filed with the SEC available on TTM's website at www.ttm.com. We've all posted -- also posted on the website a slide deck that we'll refer to during the call. I will now turn the call over to Tom Edman, TTM's Chief Executive Officer. Please go ahead, Tom.

Thomas Edman

Thank you, Sameer, and let's just make sure we're recording as well. I do want to apologize again on behalf of the company for the issues we had with this call. Unfortunately, it appears that the service provider for these calls was acquired and did not inform us of that change or the -- and did not set up the call. So my apologies for this. I hope you will bear with us here, and we'll do the best we can to respond to questions at the end of the call. So with that, let me just get started.

Good afternoon to all, and thank you for joining us for our third quarter fiscal year 2022 conference call. I'll begin with a review of our business highlights from the quarter and a discussion of our third quarter results, followed by a summary of our business strategy. Todd Schull, our CFO, will follow with an overview of our Q3 2022 financial performance and our Q4 2022 guidance. We will then open the call to your questions.

The quarter's highlights are also shown on Slide 3 of the investor presentation posted on TTM's website. In the third quarter of 2022, TTM delivered a solid quarter with revenues in line with the guided range and non-GAAP EPS above the high end of guidance despite a challenging supply chain and labor environment and the continued impact that COVID-19 is having on our business. While the results include the first -- include the first full quarter of Telephonics, I do want to call out that the rest of the company saw revenues grow 8.3% year-on-year, driven by broad-based growth across all end markets. On a year-on-year basis, we saw a significant improvement in our profit margins in Q3 from better product mix, higher pricing and premium revenue. Also the addition of Telephonics and favorable foreign exchange rates as the Chinese RMB weakened further against the dollar.

I am proud of our employees for delivering solid results this quarter. As we look into Q4, inventory adjustments and supply challenges tied to some of our commercial customers are contributing to revenue and margin declines, but we will continue to see our business supported by our diverse end market mix, including our A&D business, which, with the addition of Telephonics, now represents almost 40% of our revenues. I would now like to provide a strategic update. TTM is on a journey to transform our business to be less cyclical and more differentiated. As part of this strategic transition, near the end of the second quarter, we closed the acquisition of Telephonics.

Over the past several years, TTM has consistently emphasized that a key part of our strategy is to add value to the product solutions that we deliver to our customers, particularly in the aerospace and defense market. In 2018, we acquired Anaren, which broadened TTM's product portfolio into highly engineered RF components and subassemblies as well as adding critical RF engineering capability and resources. Telephonics builds on Anaren and TTM's customer-driven culture and disciplined approach to engineering and manufacturing by further broadening TTM's aerospace and defense product offering vertically into higher-level engineered system solutions and horizontally into the surveillance and communications markets while strengthening our position in radar systems.

The aerospace and defense end market will provide growth and stability in a potentially challenging demand environment for commercial markets. In addition, over 50% of A&D revenues will be from engineered and integrated electronic products with PCBs being less than 50% of the overall contribution. Telephonics demonstrated strong performance in their first quarter with TTM, and integration is well underway. Adding another element of our differentiation strategy is the current construction of a new state-of-the-art, highly automated PCB manufacturing facility in Penang, Malaysia. The decision to build this new factory is a direct response to our customers' increasing concerns about supply chain resiliency and regional diversification and in particular, the need for advanced multilayer PCB sourcing options in locations outside of China.

The new facility in Malaysia will assist customers in our commercial markets, such as networking telecom, data center computing and medical, industrial and instrumentation. We made great progress on the Malaysian facility this past quarter as we completed the 3,900 filings required for the building, laid the majority of the foundation and began raising the steel framework. We also received multiple deposits from customers with whom we have signed long-term agreements, which provide a business base for over 60% of the planned new capacity in the building. Recent news on increasing export controls to Chinese companies reaffirms our view of the importance of regionally diversifying for our customers' supply chain resiliency needs.

Finally, I'd like to say a few words about the overall macro environment. We are aware and understand the investor concerns of an economic slowdown and potential recession, which would mostly impact our commercial business. We will continue to closely monitor global economic influences on our commercial business. We have seen a booking slowdown in parts of our commercial business as some customers focus on managing inventories, while others continue to struggle with supply chain challenges. Our backlog continues to be robust, however, and we expect the aerospace and defense market to provide strong countercyclical element to our commercial business if conditions weaken further.

Now I'd like to review our end markets, which are referenced on Page 4 of the investor presentation on our website. The aerospace and defense end market represented 38% of total third quarter sales compared to 31% of Q3 2021 sales and 30% of sales in Q2 2022. The majority of the year-on-year growth was due to the inclusion of Telephonics. Excluding that impact, our A&D revenues grew 7.0% year-on-year. We continue to experience a positive defense climate, with our A&D program backlog at $1.16 billion, including Telephonics. Excluding Telephonics, program backlog was $871 million compared to $723 million a year ago.

This solid backlog was driven by record bookings of $319.4 million for core TTM and $387.8 million, including Telephonics. The solid demand in the defense market is a result of a positive tailwind in defense budgets and our strong strategic program alignment and key bookings for ongoing franchise programs. During the quarter, we saw significant bookings for key programs, including the Spy 6 radar program and a major space program. We expect sales in Q4 from this end market to represent about 40% of our total sales.

The medical industrial instrumentation end market contributed 19% of our total sales in the third quarter compared to 20% in the year ago quarter and 21% in the second quarter of 2022. Revenues from this market were up 18% year-on-year, exceeding $100 million for the sixth quarter in a row and performing much better than expected, with broad-based strength across all segments. For the fourth quarter, we expect MINI to be 17% of revenues as quick turn continues to moderate and select customers face component shortages.

Automotive sales represented 15% of total sales during the third quarter of 2022 compared to 18% in the year ago quarter and 18% during the second quarter of 2022. Automotive revenues grew 1.6% year-over-year and exceeded $100 million for the fourth quarter in a row. We continue to see stable trends for automotive PCBs, despite the combined impact of supply chain and demand disruptions caused by COVID, the Ukraine Russia conflict and semiconductor shortages that are all impacting automotive OEM production. We expect our automotive PCB business to contribute 16% of total sales in Q4.

Sales in the data center computing end market represented 14% of total sales in the third quarter compared to 14% in Q3 of 2021 and 17% in the second quarter of 2022. Revenues from this end market were up 18% year-on-year due primarily to growth from our data center customers. We expect revenues in this end market to represent approximately 14% of fourth quarter sales as data center demand continues to drive year-on-year growth. Networking/communications accounted for 14% of revenue during the third quarter of 2022. This compares to 16% in the third quarter of 2021 and 14% of revenue in the second quarter of 2022. We -- saw relative strength on a year-on-year basis in networking as compared to telecom as we continue to allocate capacity for high layer count boards through our data center computing and networking customers.

In Q4, we expect this end market to be 13% of revenue as customers manage their inventory levels. Next, I'll cover some details from the third quarter. This information is also available on Page 5 of our earnings presentation. During the quarter, our advanced technology and engineered products business, which includes HDI, rigid flex and RF subsystems and components, accounted for approximately 41% of our revenue and now includes all of the Telephonics revenue. This compares to approximately 29% in the year ago quarter and 33% in Q2. We are continuing to pursue new business opportunities and increase customer design engagement activities that will leverage our advanced technology and engineered products capabilities in new programs and new markets.

PCB capacity utilization in Asia Pacific was 78% in Q3 compared to 91% in the year ago quarter and 88% in Q2. Our overall PCB capacity utilization in North America was 45% in Q3 compared to 50% in the year ago quarter and 42% in Q2. The lower rate in Asia Pacific was caused by a decline in production volumes, while the lower year-over-year rate in North America was due to additional plating capacity added earlier in the year and direct labor shortages in certain regions. Our top 5 customers contributed 33% of total sales in the third quarter of 2022 compared to 30% in the second quarter of 2022. We did not have any customers over 10% in the quarter.

At the end of Q3, our 90-day backlog, including Telephonics, which is subject to cancellations, was $672.9 million compared to $594.8 million at the end of the third quarter last year, not including Telephonics and $703.7 million at the end of Q2, including Telephonics. Our book-to-bill ratio, including Telephonics, was 0.92 for the 3 months ended October 3. The book-to-bill was below 1 due to a decline in bookings in our commercial business as lead times were reduced and customers manage inventories and face supply chain challenges. I do want to thank our employees for continuing to contribute to TTM and our critical mission of inspiring innovation for our customers. Our business performed better than we expected as a direct result of our employees and our supply chain partners concerted efforts to support TTM and our customers. Now Todd will review our financial performance for the third quarter. Todd?

Todd Schull

Great. Thanks, everybody, and I appreciate your patience today with all of our technical challenges. I'll take a quick review of our financial results for the third quarter, which are also shown in the press release distributed today as well as on Slide 6 of our earnings presentation that is posted to our website. For the third quarter, net sales were $671.1 million compared to $556.8 million in the third quarter of 2021. The year-over-year increase in revenue was primarily due to the inclusion of Telephonics as well as organic growth in each of our end markets. GAAP operating income for the third quarter of 2022 was $49.8 million. This compares to $32.2 million in the third quarter of 2021. On a GAAP basis, net income in the third quarter of 2022 was $43.5 million or $0.42 per diluted share. This compares to GAAP net income of $21 million or $0.19 per diluted share in the third quarter of last year.

The remainder of my comments will focus on our non-GAAP financial performance. Our non-GAAP performance excludes M&A-related costs, restructuring costs, certain noncash expense items such as amortization of intangibles and stock compensation and other unusual or infrequent items. We present non-GAAP financial information to enable investors to see the company through the eyes of management and to facilitate comparisons with expectations and prior periods. Gross margin in the third quarter was 19.7% and compares to 17.2% in the third quarter of 2021.

The year-on-year increase was due to better product mix, higher pricing and premium revenue and the addition of Telephonics, partially offset by higher year-on-year labor costs, particularly in North America as we wages earlier this year to be more competitive. Selling and marketing expense was $19.1 million in the third quarter or 2.8% of net sales versus $15.1 million or 2.7% of net sales a year ago. Third quarter G&A expense was $38 million or 5.7% of net sales compared to $29.1 million or 5.2% of net sales in the same quarter last year. The inclusion of Telephonics added $2.3 million and $3.2 million to sales and marketing and G&A, respectively.

In the third quarter, R&D was $7 million or 1% of revenues compared to $4 million or 0.7% of revenues in the year ago quarter. $2 million of the increase was due to the addition of Telephonics. Our operating margin in Q3 was 10.2%, an outstanding result given the macro challenges we've been facing. This compares to 8.6% in the same quarter last year. Interest expense was $10.4 million in the third quarter compared to $10.6 million in the same quarter last year. During the quarter, there was a positive $9 million of foreign exchange impact below the operating line. Government incentives and interest income increased this to $10.3 million or an $0.08 impact to EPS. This compares to a loss of $0.1 million in the same quarter last year. Our effective tax rate was 15% in the third quarter, resulting in tax expense of $10.2 million. This compares to a rate of 1.1% or tax expense of $0.4 million in the prior year.

Third quarter net income was $57.9 million or $0.56 per diluted share. This compares to third quarter 2021 net income of $36.5 million or $0.34 per diluted share. Adjusted EBITDA for the third quarter was $102.5 million or 15.3% of revenue compared with third quarter 2021 adjusted EBITDA of $68.6 million or 12.3% of revenue. Depreciation for the quarter was $24 million. Net capital spending in the quarter was $26.3 million. Cash flow from operations was a very strong $80 million or 11.9% of revenue, exceeding our target of 10%. Free cash flow was also very good at $53.7 million or 8% of revenue. Cash and cash equivalents at the end of the third quarter of 2022 were $335.6 million, and our net debt divided by last 12 months EBITDA was 1.8x, below our target of 2.0.

Now I'd like to turn to guidance for the fourth quarter. We expect total revenue for the fourth quarter of 2022 to be in the range of $630 million to $670 million, and we expect non-GAAP earnings to be in the range of $0.36 to $0.42 per diluted share. As Tom mentioned earlier, we expect sequential decline in revenues due to macroeconomic concerns by customers in our commercial end markets. Some commercial customers are carefully managing inventory levels and others are facing supply chain challenges. We expect a sequential decline in margins due to lower revenues and less premium revenues. The EPS forecast is based on a diluted share count of approximately 104 million shares, which includes dilutive securities such as options and RSUs. We expect that SG&A expense will be about 9.1% of revenue in the fourth quarter and R&D to be about 1.1% of revenue. We expect interest expense to total approximately $11.7 million.

Finally, we estimate our effective tax rate to be between 13% and 17%. To assist you in developing your financial models, we offer the following additional information. During the fourth quarter, we expect to record amortization of intangibles of about $11.7 million, stock-based compensation expense of about $5.4 million, noncash interest expense of approximately $0.5 million, and we estimate depreciation expense will be approximately $24.5 million. Finally, I'd like to announce that we'll be participating in the Baird Industrial Conference on November 8 and the Bank of America Leverage Finance Conference on November 29. That concludes our prepared remarks, and now we'd like to give an opportunity for questions. Sameer?

Question-and-Answer Session

A - Sameer Desai

Yes. Thanks, Todd. This is Sameer from TTM. So if you have any questions for Tom and Todd, please text or e-mail me, and I will call on you to ask your question. [Operator Instructions] So first question, Will Stein.

William Stein

Can you hear me?

Sameer Desai

Yes, we can hear you well.

William Stein

Great. I figured it out. A couple of questions. First, you described premium revenue a couple of times in the call. I suspect that relates to sort of quick turn less than normal lead time sort of product that may be less important to customers today given the softening demand? Is that the right way to describe it?

Thomas Edman

Yes, that's correct, Will. And so it's a quick turn and generally new product introduction, that's been -- that's where a lot of that work is concentrated of late. It's -- if customers need product within -- well within our lead times, then that would be included in premium revenue. And to give you some perspective, historically, we ran about 9% of revenue and premium. And the most recent -- so if you thought think about Q2, which was very elevated, we're closer to 12%. And in this most recent quarter, we were at about 10%. So still elevated. What we're expecting in the fourth quarter is to come down actually below -- slightly below that historical average. So really seeing the pendulum come back in terms of premium requirements.

William Stein

Got it. And as a follow-up, I'd like to ask about wage inflation. This has been sort of an issue in years past where you couldn't secure enough labor. This was a supply constraint. And then earlier in the year, you talked about raising wages. I think there was a global analysis you made and you decided to raise wages globally. But I think I heard you say that you continue to be constrained by labor in North America. Is it something we should expect to continue to limit revenue growth? Or should we think about another potential wage increase on the comp?

Thomas Edman

Yes. Thank you, Will. Yes. So you're very good recollection. We -- early in the year in approximately the February time frame, we did make a very -- a big adjustment in our structures for compensation in North America. We saw that we were in a difficult labor market, and we also recognize that we have really fallen behind where we needed to be in North America. And so we -- this was part of a leveling of our entire organization. So that was a global leveling project that we did to really get all of our titling, our compensation on a global -- into a global framework, a huge project that we've embarked on several years prior. As part of that project, really the last phase was to make this adjustment in North America.

So -- and I'm pleased to say that as a result of that, of course, we also did our normal compensation review in midyear, and that is a global review. But as a result of the changes, we really have found turnover rates to come down and retention has improved. -- what we're referring to here is an ongoing challenge now is really the recruiting of labor and particularly direct labor in a number of the regions in North America that we operate in.

And that's been just an ongoing challenge that we've had to face. It's coupled a bit with ongoing absenteeism related to COVID. -- frankly, in some of the jurisdictions in which we operate, we're required to give extra PTO for -- specifically for COVID purposes, and we've chosen to do that as a company as well. So those are the 2 issues that we continue to be challenged with in North America. And I would love to say that the direct labor challenges going away. I really do think that depends on where the economy goes. We are very secure in our need for direct labor going forward and with such a strong defense business in North America that we're seeing -- we will see a need for TTM employees and continuing to build on our strong base of employees for -- certainly for the foreseeable future here in North America. Next question?

Sameer Desai

Yes. Thanks. So next question, Mike Crawford, you can go ahead and ask.

Todd Schull

You're good at reverse engineering, Mike. I'll give you credit for that. Yes, we're still going to have good margins. They just won't be as strong as our current quarter or Q3. We will still have a good performance. So if you do the reverse math, yes, you're going to probably come up with gross margins greater than 18%.

Michael Crawford

And then if I heard right regarding Malaysia perhaps you already have commitments for what would represent 60% of the capacity of that facility. So at what level of capacity do you hope to be operating that facility in general? And what do you say that -- where you are with that foundation and the steel raising that you're on track or at or behind kind of schedule to get that up and running?

Thomas Edman

Sure. Thanks, Mike. Yes. So you're correct, 60% in terms of to what would be our planned capacity. That planned capacity will be about $180 million of capacity for revenue. Of course, that will move around a little bit depending on the pricing at the given moment, what the product mix is. But that's an approximate number for you. And from a production volume standpoint, about slightly over 60% already committed to with a long-term agreement. So that's where we sit in terms of the customer side. We're continuing to work that, by the way. We continue to have some very fruitful discussions. And so hopefully, that percentage will move upwards.

In terms of progress, I think we're very much on schedule at this point. The one of the benefits in terms of the site planning that we've done in our operations team has really put in place in terms of planning. Early on, they went with a steel frame construction for this building, and that's a little bit more expensive, but it involves less labor from a construction standpoint. And Malaysia, like so many countries is dealing with labor shortages. So the fact that we've got a relatively simple and efficient construction framework is going to help us, and we certainly hope to remain on schedule to date, we are...

Sameer Desai

So next question, Jim Ricchiuti from Needham.

James Ricchiuti

Wonderful. Tom, I just wanted to drill down into not surprisingly, some of the comments about the softening you're seeing in some of your commercial markets. And I'm wondering if you could elaborate on that, which of the verticals? And how did that play out over the course of the quarter? And what are you seeing thus far in Q4?

Thomas Edman

Okay. Sure, Jim. Yes, let me -- I'll give you a bit of a ranking here. And so -- and I'll start with sort of the areas of what I would call a softening that we're seeing. If you -- if the -- the second eye in MII, which is instrumentation, so the semiconductor capital equipment side of our instrumentation business, which roughly a little bit less than half of the instrumentation piece of MII, we are seeing softness there. We are seeing softness in computing, which for us is semiconductor. -- burn-in test and burn-in board area, we've seen some relative softness there. Telecom, we've seen softness there to customers in that area are referring to inventory control, but we're believing that, that also is an indicator of a little bit of softness, the 5G build-outs right now are alive and well in India, but other countries seem to have slowed down. And then commercial aerospace continues to be weak, relatively weak. That's an ongoing story until we -- as we see passenger traffic come back as we see jet builds restart and as we see customers work through inventory, that situation should improve.

On the watch -- I'll just say, watch list, meaning customers referring to supply chain management and inventory controls, I would put data center and networking, both areas where customers are still pointing to demand strength, but they are certainly looking at short-term inventory controls as they see their supply chain situation gradually improve. So those areas in medical, I referred to a little bit of less medical premium work, which is an indicator, I think, of certainly more inventory control going on in that area as well.

So that's sort of a middling area. And then where we're still continuing to see strength. Industrial, we're involved in downhole areas, industrial robotics, big areas for us, still doing very well. Automotive solid automotive demand continues to be solid from our customers. And then, of course, defense, very strong. So a mix there of businesses. I think if you listen to that, you can see that on balance, the markets are continuing to be good with areas of softening. And those are the areas that we're watching closely.

James Ricchiuti

Got it. If I could squeeze a follow-up just with respect to telematics, and I may have missed it. Todd, I think you had talked about it contributing something on the order of $0.04 in earnings. I don't know if that was the case in the quarter and whether the synergies that you've talked about, are they -- is that time line still intact? Or it's early days, I know.

Todd Schull

I'll answer the latter first and then follow up. So in regards to synergies, as Tom indicated, we are in the process of integration, and we're making good progress -- when we announced the acquisition, we talked about our plan to achieve $12 million of run rate synergies by the end of 2024. And we are on track to deliver that. We're feeling really good about that as we get into the weeds and start being very specific in what actions to take.

So that's moving nicely and consistent with our earlier expectations. In terms of Telephonics contribution to the quarter, you're pretty close. The revenue for the quarter was about $68 million. And keep in mind that the calendar Q3 quarter is traditionally the peak quarter for Telephonics as that used to be their fiscal year-end. And so all their programs drive towards that end date.

Profit performance came in pretty good. As you noted, we give some indication, we were expecting about $0.04 of contribution. Maybe we got a little bit more than that. So it was slightly favorable, maybe $0.05, but it was in that neighborhood. So they surprised on the upside a bit there. So a good first quarter, but we are expecting things to be a little lighter in calendar Q4 as that's traditionally coming off their peak for their traditional fiscal year.

Sameer Desai

Yes. So next question, Tyler from Craig-Hallum. If we can't hear you, you might have done a year line get...

Tyler Burmeister

You may now...

Sameer Desai

Yes, I can hear you, Tyler.

Tyler Burmeister

Awesome. Great. ask a question or 2 here quick. So I guess I want to follow up on some of these commercial market weakness you're seeing. And I just wanted your thoughts there that you looking into next year, would it be fair to expect some of these headwinds to persist into next year? It would seem that off in these type of challenges and the inventory corrections and adjustments that go along with them are not use just one quarter in nature. Is that a fair way to think about as we head into the first half of next year or anything to call out there?

Thomas Edman

Yes. Thanks, Tyler. I think the -- you characterized it well. So if you go through those list of areas that I talked about as softer commercial aerospace should turn into a tailwind here as we go through the course of the next year. We've been bumping along the bottom as customers work through inventories and I expect that we'll start to see real demand come back there. I would say the same for telecom. Generally, 5G build-outs are going to continue. We should still -- we should see strength come back there. So I think really the semiconductor and semiconductor capital equipment side, those are just 2 areas I'd point out as being areas that could be weaker next year. And then the other areas, I think the jury is still out. Certainly, data center and networking. Our customers are indicating that for them, it's really a matter that their programs are strong and that they just need to work through supply chain issues. So good indicators there, at least from the customers. And then medical certainly expect that area to come back as well.

I mean, they're working through inventory, but I really do believe that's more of a temporary issue than anything else. So on balance, again, it's wonderful to have a diverse set of end markets that we're serving here, particularly in these times when certainly some areas may soften a bit. But also having that strong defense business that works on a very different cycle. So I like where we sit right now going into 2023.

Tyler Burmeister

That sounds great. And then one more quick one, if I can, for Todd, probably. On the margins, again, gross margin specifically probably, could you either maybe give us what a normalized gross margin might look like at this level, absent some of these headwinds that we called out or what kind of impact you might attribute to the gross margins in your Q4 guide, just so we can kind of get a baseline as we go into next year?

Todd Schull

I'm not sure I quite understand the question. Are you asking about Q4 guidance and expectations?

Tyler Burmeister

You talk... The Q4 guidance and you say I think margins were going to be down due to some of the same kind of macro headwinds and concerns at some of these markets we talked about. So I guess is it just a volume thing with those markets being down is there, I guess, anything else to call out on the manage front that we should be.

Todd Schull

Well, I think we made the comment in the script but it's really fairly straightforward. We have some revenue decline in Q4 compared to Q3. And really coming from some of those commercial markets, as Tom has commented on. And that hurts us in volume. But I would say, if you look at our margins overall, and we tend to look more at operating margins, but you can -- it's the same explanation for gross margins. If you do the reverse engineering of the EPS guidance that we gave, you're going to get a number somewhere around 9% in terms of operating margin, and that's down from the 10.2%. And that decline is really driven by 2 things. One, volume and the other one is a further decline in premium revenue.

So Tom talked about earlier in the call that our premium revenue in the third quarter was still pretty good. It was better than we were expecting in our guidance, and so that helped on the upside. But it is definitely declining from its peaks. And that's really a reflection of some softening that we've been talking about. So when you look at the impact in our guidance for Q4, the reason for the decline in margin is really split 50-50 lower volume and less premium revenue expected.

Sameer Desai

Thanks. So next question is Matt Sheerin from Stifel.

Matthew Sheerin

I appreciate you guys stay in and providing all these details. Just one question. I just wanted to drill down on the automotive outlook. You're still trending down year-over-year even with a sequential growth in December, and I understand the issues at your customers. But as you look at your backlog and visibility into next year, are you expecting kind of a nice rebound in growth next year?

Thomas Edman

Thanks, Matt. Yes, and I appreciate your patience -- so automotive for us, year-on-year, if you look at the fourth quarter, we'll be down sequentially maintaining very, very solid position. And I'll just remind you, last year in the fourth quarter was really when we were in the midst of a really strong rebound in customers we're building -- rebuilding inventory position. So Q4 last year was particularly strong. So as we go through the balance, we look into next year, and of course, everyone has their crystal ball. What I'm encouraged by is, number one, the overall macro trends from an automotive standpoint are going to continue to lean on electronics content. And we're going to be looking at PCB content moving from where it was at the end of last year at about $100 PCB content per vehicle upwards to, let's just say, I think the forecasters are calling for $150 to $160 by 2025.

That trend is encouraging. I think we're in the right areas as we focus on ADAS build-out as we focus on ED support. Our team has done a really good job in terms of program placement. So I'm encouraged by that. I think that will certainly help TTM overall and our positioning in the marketplace. As far as the unit volumes in automotive go, I think that's going to be a case of when the supply chain catches up. And hard to predict. Right now, our customers are still dealing with shortages. Over this last quarter, we continued to see PCB demand really robust, particularly in Europe and North America, where we saw weakness was in Asia, China and Japan. And again, I think if you look at the economics, some of the challenges in both of those economies, it makes some sense. So as we go into 2023, I think it's going to be a case of at what point does really automotive production catch up with demand. And then at that point, we'll see what real demand across our geographies is.

And so I think we're going to be, I would say, certainly in the first part of the year, we're in a solid position in automotive. And we'll see what happens again when the supply catches up. And I just can't really predict when that will happen. So -- and just while we're talking automotive, usually the question comes up. So let me address new program wins in automotive this quarter as well. We won a program value of about $125 million in the quarter off of 19 automotive designs, and that's pretty comparable to where we were last year at this time. So positive to see customers releasing packages again for new designs. So that's encouraging, particularly as those packages start to build on a strong EV story for the industry.

Sameer Desai

So this is Sameer. I don't believe we have any more questions in the queue at this point. I get to give everyone our last chance to ask any questions if they would like -- so star 6, if we can't hear you and you need to your line. Okay. It doesn't look like we have any more questions. So I'll hand it back to Tom for any concluding remarks.

Thomas Edman

Thank you, Sameer. And let me start out by thanking Sameer, acting as operator and investor relations and dealing with a very challenging vendor situation today. So thank you, Sameer, for that incredible job. And also, again, I'd like to thank all of you for your patience and your willingness to get on this call on such short notice. Let me just close by summarizing the points I made earlier.

First, TTM delivered revenues in line with guidance and earnings above the high end of guidance. Second, our end market diversification enabled strong revenue growth of 8.3% year-on-year. That's not including Telephonics. Third, we generated strong cash flow, and we're now down to a net leverage of 1.8x. And fourth, we're well positioned for whatever comes our way here in terms of the commercial markets with an aerospace and defense business at 40% of revenues. So in closing, I would just like to thank our employees and our customers. And of course, you, our investors, for your support and your ongoing support. Thank you very much. I hope you have a good rest of the day.