1st Quarter 2015 Earnings Conference Call Transcript



April 30, 2015

Overview*:

BDC reported 1Q15 consolidated revenues of $569.5M, income from continuing operations of $43.3M and diluted EPS from continuing operations of $1.00. Belden expects FY15 revenue to be $2.450 - 2.500B and adjusted diluted EPS from continuing operations to be $5.28 - 5.48. Belden expects 2Q15 revenue to be $605-625M and adjusted diluted EPS from continuing operations to be $1.15 - 1.25.

*Adjusted results. See appendix for reconciliation to comparable GAAP results

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CORPORATE PARTICIPANTS

John Stroup Belden, Inc. - President, CEO
Henk Derksen Belden, Inc. - CFO, SVP-Finance
Matt Tractenberg Belden, Inc. – VP, Investor Relations

PRESENTATION

Matt Tractenberg Belden, Inc. – VP, Investor Relations

Thank you, operator. Good morning, everyone, and thank you for joining us today for Belden's first quarter, 2015 earnings conference call.

My name is Matt Tractenberg and I am Belden's Vice President of Investor Relations. With me here this morning are John Stroup, President and CEO, and Henk Derksen, Belden's CFO. John will provide a strategic overview of our business, and then Henk will provide a detailed review of our financial and operating results, followed by question and answer.

We issued our earnings release earlier this morning, and we have prepared a slide presentation that we will reference on this call. The press release, presentation, and transcript of these prepared remarks are currently available online at investor.belden.com.

Turning to slide two in the presentation. During this call management will make certain forward looking statements. I would like to remind you that any forward looking information we provide is given in reliance upon the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995. The comments we will make today are management's best judgment based on information currently available. Actual results could differ materially from any forward looking statements that we make, and the Company disclaims any obligation to update this information to reflect future developments after this call. For a more complete discussion of factors that could have an impact on the company's actual results, please review today's press release and our annual report on Form 10-K.

Additionally, during today's call management will reference adjusted or non-GAAP financial information. In accordance with Regulation G, we have provided a reconciliation of the most closely associated GAAP financial information to the non-GAAP financial information we communicate. This reconciliation is in the appendix of the presentation and has been posted separately to the investor relations section of our Web site.

Before we begin, I'd like let our investors and analysts know that we'll be holding a live event in Montreal on June 4th, that will focus on the Broadcast platform here at Belden. We'll discuss the market, the technology, speak with customers, and walk through a studio demo. We'll also be touring our factory floor. If you'd like to join us, you can register right on our website at investor.belden.com, under the news and events section, just click the link that says Broadcast Day.

I will now turn the call over to our President and CEO, John Stroup. John?

John Stroup Belden, Inc. – President, CEO

Thank you, Matt, and good morning, everyone.

As a reminder, I'll be referring to adjusted results today.

Please turn to slide three in our presentation for a review of our first quarter highlights.

Given the macroeconomic challenges facing all global companies, I am especially pleased with our results for the first quarter. I believe it is the direct result of a purposeful approach to creating a strong and balanced portfolio in combination with solid and steady execution. I'd like to thank all our associates for their hard work during the quarter, and their commitment to aggressively executing our strategic plan.

Total revenues for the first quarter were $569.5 million, an increase of 16.6%. On a constant currency basis, total revenues increased 22.5%. The stronger U.S. dollar had an approximate $29 million unfavorable impact on revenues, and revenues grew 2.4% on an organic basis.

The demand environment in the first quarter varied by market and geography. As you would expect, revenue growth was strongest at Tripwire, our newly acquired Network Security platform. A pleasant and, somewhat surprising, result was a return to organic growth at our Enterprise platform. Although forecasted in 2015, it came a little earlier than expected. Both of our industrial platforms posted organic growth in excess of 3%, despite overcoming challenges with weak demand in Brazil. Meanwhile, after an exceptionally strong 2014 and in particular, fourth quarter, our Broadcast segment battled the realities of a stronger U.S. dollar. In particular, our Grass Valley business had to overcome year-over-year revenue declines in the Middle East, Russia and Latin America. As a result, revenue in our Broadcast platform was flat year-over year on an organic basis.

From a geographic perspective, we continue to benefit from a diversified global footprint. We experienced solid performance across several regions, with notable strength in the US and Canada, up 5.9%; and western Europe, up 5.1%; both on an organic basis, more than offsetting continued weakness across several emerging markets, which experienced a contraction of almost 9% from the year-ago period.

Record gross profit margins were 40.6% during the quarter, an increase of 450 basis points from the year-ago period. In addition to being best in class, these margin levels allow us to further leverage our organic growth initiatives.

Operating profit margins in the first quarter were 13.5%, a year-over-year increase of 40 basis points. EBITDA margins were 15.5%, also an increase of 40 basis points from the year-ago period.

We generated earnings per diluted share of $1.00 in the first quarter, an increase of 25% from the year-ago period.

And finally, we completed the acquisition of Tripwire, a leading provider of innovative cybersecurity software. We've spoken to you about the pervasive needs of customers across Enterprise, Industrial, and Broadcast markets to protect their mission-critical infrastructure. The Network Security platform will comprise a fifth business segment for Belden, and we believe it makes sense to report these results separately.

Please turn to slide four for a review of our business segment results.

Broadcast revenue in the quarter was $213.6 million dollars as compared to $166.5 million in the year ago period, an increase of 31.2%, and a result of, among other things, the acquisition of Grass Valley. Revenues, on an organic basis, were flat during the period and in line with the market. EBITDA margins were 13.7%, decreasing 200 basis points year-over-year, a result of mix within the portfolio as strength in Broadband connectivity partially offset the impact of recent acquisitions. I am extremely pleased with the progress made with the integration of Grass Valley. In particular, response to our new end-to-end IP solution at the most recent NAB show was encouraging. Although our customers are managing through a number of uncertainties regarding their business model and technology adoption, we are better positioned than anyone to help them successfully navigate this period of disruption. And I believe they greatly appreciate our vast experience with IP transitions in mission critical applications; something our competition can't offer them.

The Enterprise platform returned to growth with revenues of $104.7 million, an increase of 4.2% year-over year on an organic basis. I'm encouraged by the strength we're seeing in the market, with solid results in all geographies. I'm especially pleased with growth of almost 18% from our connectivity portfolio; a sign that the hard work of focusing the business on higher value solutions is delivering the desired results. We'll continue to monitor the business environment, but we anticipate continued growth from the platform as we make our way through the year. Profitability was also strong, with EBITDA margins of 13.3% during the quarter, an increase of 20 basis points from the year-ago period.

Industrial Connectivity had revenue for the quarter of $153.0 million, an increase of 3.2% organically. EBITDA margins were 15.8% for the first quarter, up 90 basis points. Coast, an acquisition completed last fall, continues to perform well, already delivering ROIC in excess of 11%.

Industrial IT revenue of $61.1 million increased by $7.0 million from $54.1 million in the first quarter of 2014. After adjusting for changes in currency, revenues increased 4.0% year-over-

year, on an organic basis. EBITDA margins of the platform were 18.2%, an increase of 50 basis points from the year-ago period. I'm proud of our team's recent recognition by Frost and Sullivan, a well-respected industry research firm, for outstanding leadership in product line strategy. In particular, they noted how our thoughtful approach to acquiring and integrating businesses, in combination with leading product innovation and global market coverage, provides customers with the most comprehensive industrial IT solution.

Network Security contributed revenues of $37.1 million, an increase of 20.7% year-over-year. EBITDA margins were 26.7%, an exceptional first quarter in the Belden portfolio. As you've likely seen in the media, security breaches continue to occur at an alarming rate. Recently, we've seen a number of them within industrial, and even broadcast markets. This helps to illustrate that now, more than ever, our customers need to protect their mission critical infrastructure. For those of you who'd like a deeper dive into their products, markets, and opportunities, we've recently posted an educational webcast on the IR homepage at Investor.Belden.com.

I will now ask Henk to provide additional insight into our first quarter financial performance. Henk?

Henk Derksen Belden, Inc. - CFO, SVP-Finance

Thank you, John. I will start my comments with results for the quarter, followed by a review of our segment results, a discussion of the balance sheet, and close with our cash flow performance. As a reminder, I will be referencing adjusted results today.

Please turn to slide five for a detailed consolidated review**.** First quarter revenues were $569.5 million dollars. Compared to the first quarter 2014, revenues grew 16.6%, or 22.5% on a constant currency basis, from $488.3 million. Acquisitions contributed $106.7 million in the quarter and were partially offset by foreign currency translation headwinds of $28.5 million, as a result of the stronger US dollar. Revenues in the first quarter increased 2.4% year-over-year, on an organic basis, a result of the solid performance in our Enterprise and Industrial platforms.

Sequentially, revenues decreased $44.2 million dollars from $613.7 million as the unfavorable effects of normal seasonality and foreign currency headwinds were partially offset by revenues from acquisitions.

Gross profit margins were at an all-time record of 40.6%, increasing 450 basis points from the year-ago period and 320 basis points sequentially, a result of successful execution on our M&A strategy.

First quarter SG&A expenses were $119.9 million dollars, or 21% of revenue. After adjusting for currency and acquisitions, SG&A expenses declined $4.0 million, or 80 basis points, from the year-ago period due to the productivity improvement program implemented in prior year.

R&D expenses for the quarter were $34.8 million dollars, or 6% of revenue. This represents an increase of 200 basis points year-over-year as a percentage of revenues and illustrates the shift to more innovative products and services.

EBITDA margins were 15.5%, up 40 basis points year-over-year and down 80 basis points sequentially. Operating profit margins were 13.5%, up 40 basis points year-over-year and down 100 basis points sequentially. The year-over-year increases are due to the productivity improvement programs initiated last year while the sequential declines are a result of typical seasonal revenue patterns.

Net interest expense for the quarter was $23.8 million dollars, an increase of $5.2 million year-over-year, a result of the additional senior subordinated notes issued in June and November of 2014. Given current exchange rates, our capital structure provides for an expected interest expense of approximately $25.5 million dollars per quarter going forward.

The adjusted effective tax rate for the first quarter was 18.8% compared to 21.9% in the prior year. For financial modeling purposes, we continue to recommend using a 20% effective tax rate for the second quarter 2015 and full year.

Income from continuing operations per diluted share increased 25% from the year-ago period to $1.00 per share in the first quarter 2015.

Please turn to slide six. I will now discuss revenues and operating results by business segment.

Broadcast Solutions generated revenues of $213.6 million dollars during the first quarter. Compared to the year-ago period, revenues increased $47.1 million, or 28.3%, from $166.5 million. Organic revenues are flat on a year-over-year basis following a strong performance in the fourth quarter of 13.2% organic growth. The first quarter was impacted by lower demand in certain emerging market regions, including the Middle East, Russia, and Latin America in response to currency and geopolitical related pressures.

EBITDA margins of 13.7% within the Broadcast segment decreased 200 basis points year-over-year and 340 basis points sequentially. The year-over-year comparison is impacted by the inclusion of Grass Valley, and the sequential decline, a function of lower volume.

Our Enterprise Connectivity Segment generated revenues of $104.7 million dollars during the first quarter, decreasing $3.7 million year-over-year. Revenues increased 4.2% year-over-year, on an organic basis, with solid growth across all applications.

EBITDA margins increased 20 basis points year-over-year and sequentially due to improved product mix.

Our industrial platforms are performing in line with expectations with organic growth of 3.4%.

The Industrial Connectivity Segment generated revenues of $153.0 million dollars during the first quarter. Organic revenue growth of 3.2% on a year over year basis includes the softness experienced within oil and gas markets in Brazil with an impact of more than 200 basis points.

EBITDA margins of 15.8% increased 90 basis points year-over-year and 60 basis points sequentially largely due to the accretive acquisition of Coast and productivity.

The Industrial IT segment generated revenues of $61.1 million dollars during the first quarter. Revenues increased $7.0 million year-over-year with acquisitions contributing $12.3 million and were partially offset by $7.5 million of currency headwinds. Revenues increased 4.0%, on an organic basis, compared to the year-ago period with solid growth from our global automation partners.

EBITDA margins of 18.2% increased 50 basis points year-over-year and declined 270 basis points sequentially. The year-over-year improvement is primarily due to productivity improvements while the sequential decline is a result of lower volume.

Finally, our new Network Security platform generated revenues of $37.1 million dollars in the first quarter. The team delivered a strong performance, with better than expected growth of approximately 21% compared to the prior year period. We are encouraged by the strong start, and we will continue to provide insight into the business as we make our way through the year. EBITDA margins in the first quarter were 26.7%. Both the year-over-year growth and EBITDA margins highlight the significant accretion that Tripwire brings to the business model.

If you will please turn to slide seven, I will begin with our balance sheet highlights.

Our cash and cash equivalents balance at the end of the first quarter was $167 million dollars compared to $570 million in the prior year. The decrease is primarily due to the acquisition of Tripwire closed at the beginning of this year.

Inventory turnover was 5.7 turns, flat on a year-over-year basis.

Days sales outstanding was 63 days in the first quarter, an increase of 6 days year-over-year.

Working capital turnover was 6.2 turns, an improvement of 0.2 turns year-over-year. We expect each of these metrics to improve throughout the year as acquisitions continue to benefit from our proven LEAN enterprise system.

PP&E turnover was 6.9 turns, an improvement of 0.4 turns year-over-year. We continue to generate significant improvement in fixed asset efficiency due to our lean enterprise initiatives.

Our debt balance increased $530 million dollars from $1.37 billion in the first quarter 2014 to $1.90 billion in 2015 due to the additional senior subordinated notes issued in June and

November last year. Additionally we used $200 million of capacity on our revolver to complete the acquisition of Tripwire.

Net leverage increased to 3.8 times net debt to EBITDA, slightly ahead of our plan due to the favorable impact of foreign currency on our Euro-denominated debt. Our goal of improving this metric to a level of approximately 3.0 by the end of the year remains intact.

Please turn to slide eight for a few cash flow highlights.

The first quarter resulted in a use of cash in operations of $48.2 million dollars compared to a use of cash of $20.4 million in the prior year period. Net capital expenditures for the quarter were $15.5 million, increasing $5.1 million compared to last year.

Free cash flow was negative ($63.7) million in the first quarter 2015 compared to negative ($30.8) million in the prior year period. The first quarter 2015 was impacted by $31 million of non-recurring costs and investments related to acquisitions and $5 million of additional interest expense from notes issued last year.

In the first quarter, we deployed $710 million dollars to the acquisition of Tripwire, consisting of both consideration and equity-related compensation. This results in excess of $1 billion deployed towards strategic acquisitions over the last 12 months. I am pleased with our ability to continually identify attractive capital deployment opportunities.

That completes my prepared remarks. I would now like to turn this call back to our CEO, John Stroup, for the outlook. John?

John Stroup Belden, Inc. – President, CEO

Thank you, Henk.

Please turn to slide nine for our outlook regarding the second quarter and full year 2015 results, which have been updated to reflect current exchange rates.

We expect second quarter 2015 revenues to be between $605 and $625 million, and adjusted income from continuing operations per diluted share is expected to be between $1.15 and $1.25.

For the full year, we now expect revenues between $2.450 and $2.500 billion. As a result of the stronger U.S. dollar, the expected range of adjusted income from continuing operations per diluted share is now at $5.28 to $5.48, which represents earnings growth between 25% and 30%.

That concludes our prepared remarks. Operator, please open the call to questions.