

1st Quarter 2022 Earnings Transcript

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CORPORATE PARTICIPANTS

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PRESENTATION

Kevin Maczka Belden, Inc. – VP, Investor Relations & Treasurer

Thank you, operator. Good morning, everyone, and thank you for joining us today for Belden's first quarter 2022 earnings conference call.

My name is Kevin Maczka, I'm Belden's Vice President of Investor Relations and Treasurer. With me this morning are Belden's President and CEO Roel Vestjens and Senior Vice President and CFO Jeremy Parks. Roel will provide a strategic overview of our business, and then Jeremy will provide a detailed review of our financial and operating results, followed by Q&A.

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 2 in the presentation. During this call management will make certain forward-looking statements. For more information, please review today's press release and our most recent 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, the appendix to our presentation and the investor relations section of our website contain a reconciliation of the most closely associated GAAP financial information to the non-GAAP financial information we communicate.

I will now turn the call over to our President and CEO Roel Vestjens. Roel?

Roel Vestjens Belden, Inc. – President & CEO

Thank you, Kevin, and good morning, everyone. As a reminder, I'll be referring to adjusted results today.

Please turn to Slide 3 for a summary of today's presentation.

We delivered another outstanding quarter with total revenues and EPS that exceeded expectations. I'd like to thank our global teams for their extraordinary work to navigate a complex operating environment, support our customers, and execute our strategic plans.

Demand trends remained robust in the first quarter. Revenues increased 19% on an organic basis and record incoming order rates resulted in a very strong book to bill ratio of 1.27 times.

During the quarter we further strengthened and de-levered our balance sheet. Solid EBITDA growth and $350 million in gross proceeds from the Tripwire divestiture resulted in a reduction in net leverage to 1.6 times at the end of the first quarter 2022, compared to 4.1 times a year ago. We are very pleased to report such meaningful improvement over the last year.

This was also a very active period for capital deployment. Consistent with our balanced capital deployment strategy, we executed the following accretive initiatives.

First, we completed three strategic bolt-on acquisitions for a combined purchase price of $85 million, including two during the first quarter in the Industrial Automation market and one subsequent to quarter end in the Broadband and 5G market. We are excited about the growth and value creation potential of these acquisitions, and I will provide additional details on them on the following slide.

Second, we redeemed the full 200 million Euros outstanding on our 2026 notes. This lowered our gross leverage level and interest expense, and pushed the first debt maturity to 2027.

Third, we repurchased approximately 885,000 shares for $50 million under our existing authorization.

Finally, we increased our full year guidance to reflect better than expected performance in the quarter, an improved outlook for the remainder of the year, and the accretive capital deployments. For the full year 2022, we are increasing the high end of our revenue and EPS guidance ranges by $90 million and $0.50, respectively. We are very well positioned to deliver on our commitments to shareholders and drive sustainable growth.

In summary, this was another excellent quarter for Belden, and I am very proud of the achievements of our teams. We continue to transition Belden from a supplier of trusted products to a value-added partner in the design and implementation of comprehensive networking solutions. We are making great progress, which is reflected in our strong financial performance.

Now, before we review our first quarter performance in more detail, let's discuss our recent acquisitions.

Now please turn to Slide 4 in the presentation.

As I mentioned, we completed three acquisitions year to date in 2022.

This included Macmon Secure GmbH in January for $42 million, which will be reported in our renamed Industrial Automation Solutions segment. We believe this new name better reflects the configuration of the business following the Tripwire divestiture.

As discussed on the fourth quarter earnings call, Macmon is a leader in advanced network access control software. Its products are complementary to Belden's leading industrial networking portfolio and will be integrated with our Hirschmann offering to expand our ability to provide complete end-to-end solutions. Key vertical markets include automotive manufacturing, food & beverage, utilities, and healthcare.

More recently, we acquired NetModule AG in March for $24 million. NetModule, which will also be reported in the Industrial Automation Solutions segment, is a leading manufacturer of wireless communication products for the rapidly growing mass transit market. The company uses the latest wireless technologies, including 5G and WiFi6, to support hybrid wired and wireless applications in this market. Its products will also be integrated into Belden's industrial networking portfolio to support complete end-to-end solutions.

Finally, we acquired Communication Associates Inc., or CAI, subsequent to quarter end for $19 million. CAI will be reported in the Enterprise Solutions segment. It provides a range of products used in broadband Hybrid Fiber Coax networks. CAI's products are approved by major cable providers for the upgrade cycle to new DOCSIS 4.0 standards and to support 5G backhaul. This acquisition fills a gap in our broadband & 5G product offering, and further expands our strategic partnership with MSO customers.

In each case, these acquisitions add important technologies, complement our capabilities, and enhance our ability to provide comprehensive solutions to customers. We are very pleased to add these talented teams and innovative technologies to our portfolio.

On a combined basis, we expect these businesses to contribute approximately $30 million in revenue in 2022. Once fully integrated, we see numerous opportunities to drive substantial growth and healthy returns on these investments as we leverage our global customer base and solution-selling capabilities.

We are prioritizing organic growth, but we continue to pursue other strategic acquisitions like these to further enhance our product offering and growth potential.

Please turn now to Slide 5 for a review of an innovative new product.

We continue to make targeted investments throughout the Company to develop new and innovative products that support our solution-selling strategy.

One new product that I'd like to highlight in the industrial automation market is a new family of next-generation network switches called Bobcat.

This product is ruggedized and approved for use in the most demanding and mission-critical industrial environments. Bobcat combines a compact package with high performance. It incorporates market-leading technology to address expanding networks, real time control through time-sensitive networking, higher bandwidth, and increased security. It is a powerful platform that adapts to customers evolving requirements in markets such as consumer packaged goods, food & beverage, material handling and automotive manufacturing.

We expect to continue developing innovative new products and complete networking solutions to support our customers and increase our growth opportunities.

Now please turn to Slide 6 in our presentation for a review of the first quarter highlights.

We delivered meaningful growth and margin expansion again this quarter.

First quarter revenues increased 20% year over year to $610 million, exceeding our guidance range of $558 to $573 million. Organic growth is a top priority, and revenues increased 19% year over year on an organic basis.

Our strong performance was broad based across both the Industrial Automation Solutions and Enterprise Solutions segments.

Orders increased 33% year over year to a new record level, resulting in a book to bill ratio of 1.27 times.

EBITDA increased 30% year over year to $99 million. EBITDA margins expanded 130 basis points, from 15.0% in the year-ago period to 16.3%.

EPS increased 46% year over year to $1.31, compared to $0.90 in the year-ago period and our guidance range of $1.03 to $1.13.

We are off to a great start in 2022, and we are increasing our guidance for the year.

This revised guidance now implies consolidated organic growth of 7% to 9%, compared to our prior expectation of 4% to 6%.

We also reduced net leverage to 1.6x, and completed the early redemption of our 200 million Euro 2026 notes.

Turning now to our key strategic markets. We had another great quarter in industrial. Industrial Automation revenues increased 21% organically in the first quarter.

Market conditions remain very healthy, and we continue to see a number of compelling longer-term demand drivers for automation solutions as industrial customers respond to increasing labor costs, capacity and productivity requirements, and repositioning of manufacturing footprints and supply chains. Belden is highly differentiated in the marketplace, and we expect to deliver solid growth in this market going forward.

Enterprise revenues increased 17% year-over-year on an organic basis in the first quarter, driven by improving end market trends and share capture.

Within the segment, revenues in Smart Buildings increased 17% organically. We are very encouraged by the trends we are seeing in this market and the strong execution by our teams. We are also benefitting from our commercial focus on growth verticals, such as data centers, government, and healthcare facilities.

Revenues in Broadband and 5G increased 16% organically, driven by strong demand for our fiber connectivity products. We see long-term secular trends in this market driven by the ever-increasing demand for high-speed broadband and the investments required to upgrade existing cable networks and build out new wireless networks. We have sustainable competitive advantages in this market, and we are ideally suited to support both MSO and Telco customers as they continuously upgrade and expand their networks.

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

Jeremy Parks, Belden, Inc. - CFO

Thank you, Roel.

Please turn to Slide 7 for a detailed consolidated review.

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

Revenues were $610 million dollars in the quarter, increasing $102 million, or 20%, from $509 million in the first quarter of 2021.

Revenues increased 19% year over year on an organic basis.

Record incoming order rates increased 33% year over year and 7% sequentially compared to the strong orders in the fourth quarter 2021.

This resulted in a book to bill ratio of 1.27 times, including 1.40 in Enterprise and 1.16 in Industrial Automation.

Gross profit margins in the quarter were 34.6%, increasing 100 basis points compared to 33.6% in the year-ago period. We continue to proactively address market inflationary pressures through price recovery and productivity measures to support gross profit margins.

EBITDA was $99 million dollars, increasing $23 million, or 30%, compared to $77 million in the prior-year period.

EBITDA margins were 16.3%, increasing 130 basis points compared to 15.0% in the year-ago period, demonstrating solid operating leverage on higher volumes.

We generated healthy incremental EBITDA margins, as our teams continue to execute well in this challenging inflationary and supply chain environment.

Net interest expense declined $1 million from the year-ago period, reflecting favorable foreign exchange rates.

Following the early debt repayment that we completed in the first quarter, we now expect interest expense to be approximately $50 million in 2022, compared to $63 million in 2021.

Our effective tax rate was 19.5% in the first quarter. We expect an effective tax rate of approximately 20% for the remainder of 2022.

Net income in the quarter was $59 million dollars, compared to $40 million in the prior-year period.

Earnings per share was $1.31, increasing 46% compared to $0.90 in the first quarter 2021.

We were very pleased to deliver such robust growth and margin expansion again this quarter.

Turning now to slide 8 in the presentation for a review of our business segment results.

I will begin with our Industrial Automation Solutions segment.

As a reminder, our Industrial solutions allow customers to transmit and secure audio, video and data in harsh industrial environments. Our key markets include discrete manufacturing, process facilities, energy, and mass transit.

The Industrial Automation Solutions segment generated revenues of $342 million dollars in the quarter, increasing 21% from $282 million in the first quarter of 2021. Segment revenues also increased 21% on an organic basis, with double-digit growth in each of our primary market verticals.

Industrial Automation segment EBITDA margins were 19.7% in the quarter, increasing 280 basis points compared to 16.9% in the year-ago period, due to solid operating leverage on volume growth and favorable pricing.

Turning now to our Enterprise segment. Our Enterprise solutions allow customers to transmit and secure audio, video and data across complex enterprise networks. Our key markets include smart buildings, and broadband and 5G.

The Enterprise Solutions segment generated revenues of $268 million dollars during the quarter, increasing 19% from $226 million in the first quarter of 2021. Segment revenues increased 17% organically, with similar growth in both Smart Buildings and Broadband and 5G.

Revenues in the Smart Buildings market increased 17% year-over-year on an organic basis. Improving market conditions and strong operational performance resulted in further share capture during the quarter.

Revenues in Broadband and 5G increased 16% year-over-year on an organic basis due to solid share capture and especially strong demand for our fiber connectivity products. The book to bill was 1.75 times in broadband fiber, and we expect solid double-digit growth in these products in 2022.

Enterprise Solutions segment EBITDA margins were 11.5% in the quarter, compared to 12.5% in the prior year period. To support accelerating demand and keep our customer commitments, we expedited delivery of certain input materials during the quarter. We view the associated cost pressure as temporary and expect margins to increase going forward.

If you will please turn to Slide 9 for our balance sheet highlights.

Our cash and cash equivalents balance at the end of the first quarter was $560 million dollars compared to $642 million in the fourth quarter and $369 million in the first quarter 2021.

Days sales outstanding of 57 days were consistent with the prior quarter and the prior-year period.

Inventory turns were 4.1, compared to 4.7 in the prior quarter and 4.9 the prior-year period. Our inventory levels increased during the quarter as we proactively managed supply chain challenges and prepared to support the robust expected growth throughout 2022.

Our financial leverage improved again this quarter. Net leverage of 1.6 times net debt to EBITDA at the end of the first quarter is significantly reduced from 2.1 times in the fourth quarter and 4.1 times a year ago.

During the first quarter, we repurchased approximately 885,000 shares for $50 million. Following these repurchases, we have $165 million remaining on our existing authorization.

Going forward, we intend to maintain a disciplined financial policy. Our capital allocation priorities will be balanced, emphasizing organic growth initiatives while also considering strategic M&A and additional share repurchases.

Turning now to slide 10. I will now discuss our debt maturity schedule.

As a reminder, our debt is entirely fixed at attractive interest rates. We have no near-term maturities and no maintenance covenants on this debt.

During the quarter, we took steps to further strengthen and de-lever the balance sheet. Specifically, in March we redeemed the full 200 million Euros outstanding on our 2026 notes. These were our highest interest rate notes at 4.125%.

As a result, our debt maturities now range from 2027 to 2031, with an average interest rate of 3.5%. This provides significant financial flexibility as we execute our strategic plans.

Please turn to Slide 11 for a few cash flow highlights.

Total cash flow from operations in the first quarter was a use of $58 million dollars, compared to a use of $42 million in the prior-year period.

Net capital expenditures were $11 million for the quarter, consistent with the prior-year period.

Free cash flow in the quarter was a use of $69 million dollars, compared to a use of $53 million in the prior-year period.

Free cash flow was impacted by one-time transaction costs during the quarter related to the Tripwire divestiture. The underlying cash flow performance of the business was consistent with our expectations and typical seasonal patterns.

For the full year 2022, we expect free cash flow to exceed $200 million.

That concludes my prepared remarks. I would now like to turn the call back to our President and CEO, Roel Vestjens, for the outlook. Roel?

Roel Vestjens, Belden, Inc. – President & CEO

Thank you, Jeremy.

Please turn to Slide 12 for our outlook.

The market environment is very dynamic with considerable challenges and uncertainties. However, our demand trends are very robust and our global teams are performing at a high level. We are executing our strategic growth plans and have positioned the Company for further solid growth and margin expansion in 2022 and beyond.

At current copper prices and foreign exchange rates, we anticipate second quarter 2022 revenues of $625 million to $640 million, and EPS of $1.35 to $1.45.

We now expect full year 2022 revenues of $2.48 billion to $2.53 billion, compared to prior guidance of $2.39 billion to $2.44 billion.

We now expect full year 2022 EPS to be $5.55 to $5.85, compared to prior guidance of $5.00 to $5.35. Our revised guidance now implies consolidated organic growth of 7% to 9%, with solid growth in both segments, compared to our prior expectation of 4% to 6%.

The Macmon acquisition was contemplated in the prior guidance, and we now anticipate an incremental $17 million revenue contribution in 2022 from the NetModule and CAI acquisitions.

We also expect an incremental $0.13 from lower interest expense and $0.09 from lower share count following the early debt repayment and share repurchase activity in the first quarter.

For the full year 2022, our new guidance implies total revenue growth of 8% to 10%, and EPS growth of 17% to 23%.

Please turn to slide 13.

Before we conclude, I would like to reiterate that I am extremely optimistic about our future. We entered 2022 with significant momentum and delivered an exceptional first quarter. Our strategic growth initiatives continue to gain traction, and I am encouraged by our recent order rates and the execution of our teams across the Company.

Belden is well positioned to benefit from the favorable secular trends in industrial automation, broadband & 5G, and smart buildings. I am confident that our team will continue to deliver robust organic growth and margin expansion, driving significant value for our shareholders.

Finally, I would like to announce that we are planning to host Belden's 2022 investor day event in person at the New York Stock Exchange on the morning of June 15th. Additional details and registration information will be available shortly on our investor relations website. It should be a very informative event, and we look forward to seeing you there.

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