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Flex Ltd. (FLEX)

Investor Day

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MANAGEMENT DISCUSSION SECTION

Operator: Good afternoon and welcome to the Flex 2020 Investor and Analyst Webcast and Conference Call. Today's call is being recorded and all lines have been placed on mute to prevent any background noise. After the speakers' remarks there will be a question-and-answer session. At this time, for opening remarks, I would like to turn the call over to Mr. David Rubin, Flex's Vice President of Investor Relations. Sir, you may begin.

David Rubin
Vice President, Investor Relations, Flex Ltd.

Good day and thank you for joining Flex's fiscal 2020 investor and analyst webcast. First, couple of housekeeping items, slides for today's discussion are being presented on the Investor Relations section of our flex.com website. The full deck along with an appendix containing a detailed reconciliation between GAAP and non-GAAP financial results we made available on our website. Today's webcast includes forward-looking statements which are based on current expectations and assumptions and may change. We undertake no obligation to update these forward-looking statements, so for a full discussion of the associated risks and uncertainties please see our most recent filings with the SEC.

Our presentation will be approximately one hour before we conclude with Q&A. We will give a brief update on the situation surrounding the coronavirus outbreak, and then move to our long-term strategy discussion both led by our Chief Executive Officer, Revathi Advaithi. Next we'll discuss our segment strategies and structure with Group

Presidents, Doug Britt and Paul Humphries. Finally, we will dive into our financial framework discussion led by Chief Financial Officer, Chris Collier.

With that, I'd like to turn the call over to our CEO, Revathi.

Revathi Advaithi

Chief Executive Officer & Director, Flex Ltd.

Thank you, David. Good morning, everyone. We had really hoped to join all of you in New York today, but however given the unusual nature of the current environment we felt it was more important that people's safety and well-being came first. So for today's agenda we have cut short a very extensive presentation we had planned for all of you to a few critical areas of our strategic thinking. Despite all the noise in the economy we chose to present our story to you because I'm confident about our strategy in any environment. We are making many changes, and the magnitude of these changes position us well for the long term. As you would expect, I want to start first with an update on COVID-19, what we have done and what we are doing as the crisis continues to unfold.

While this situation is challenging, I want you to understand that Flex's strategy and direction should make us even stronger in executing under difficult circumstances like this. As we mentioned in Monday's press release, we issued our fourth quarter fiscal 2020 guidance on January 30th, excluding any potential impact from the virus. It was early in the outbreak and it was evolving very rapidly. This situation continues to remain very dynamic on a global scale, and for us with several weeks left in the quarter it is still not prudent to give you a number. Many of you who have talked to understand and agree with the situation, particularly because outside of China we're only seeing the situation unfold right now. Because of this we'll postpone giving you our fiscal year 2021 guidance until our position becomes clearer in the near future.

But it's important that we explain the framework of how we're aggressively managing the situation and we're committed to being good stewards of our capital. So as soon as the COVID-19 situation started, we deployed our contingency and resiliency plan in a very disciplined way. The first phase of our plan was focused on getting our people safe. The most important thing that we can control is how we protect our people and create a safe environment for them to return to work. So once we have the right data and deployed rigorous safety measures, we identified the appropriate ways we could ramp and operate under the utmost safety. We systematically deployed teams and defy work streams, we set up war rooms with thousands of employees organizing across the globe. We have been very focused on communicating and coordinating with our customers.

At the leadership team level, plans are being reviewed and redirected daily and weekly as required. Two weeks ago, the main challenge we were working through was the supply chain in China. However, the situation is improving quickly. This week, the challenge is understanding what is happening city by city across the world and which of our factories could be impacted next. Our China playbook for this situation has been so strong and so effective that we're using the same process at all of our other locations. We have looked forward and we have built contingency plans for many varied and extraordinary scenarios, and we are deploying them on an as needed basis.

All of this has resulted in 90% plus percent of our colleagues in China returning back to work. We're also seeing significant improvements in our component shortages and impacted suppliers in China. I have to say I'm personally very proud of our teams and our disciplined execution in such extraordinary times.

So as we do our best to look forward, we're being prudent in our planning assumptions and assuming that will take at least two or more quarters for our end markets to work through the impact of this situation. Of course, as you all would know, this is not easy to predict, but my goal is always to plan cautiously in these uncertain times. While the COVID-19 issue is challenging to everyone, our goal when we look back on this time is that Flex provided the most coordinated and effective response to all of our stakeholders. As we walk through our strategic direction, it'll be clear to you as to why we have confidence in this approach.

So I'm not going to go into a lot of detail on this slide to talk to you about what we have accomplished in the last year. It has obviously been a very busy one for us. We have done a lot in a short amount of time and our results have demonstrated this progress. Not only have we created a framework and a playbook that's differentiated for this industry, but our performance this year has shown that our approach will work.

For those of you who are new to Flex, here's a quick snapshot of our business and how we are positioned today. I'm not going to go through it. You can read it yourself.

So we have a strong history, a history that's built on technology and manufacturing differentiation, and that has set the pace for this industry. So as we reflected on this history and where we want to go, we're really focused on a few key questions, like, do we need to do something different, or what is the core of our business today. We all agreed that we have the opportunity to reposition our core and rethink our growth strategy.

These discussions led to some very important shifts in our vision, our mission and our purpose. Our purpose is to make great products for our customers that create value and improve people's lives. We already do a lot to improve people's lives either in places where we create economic growth through our factories or where our products contribute to improving the environment. And we memorialize this in our purpose. So we can clearly state that we won't be opportunistic in our growth and book businesses that don't meet our core purpose.

This perfectly leads to talking about our team's outstanding work around the topic of ESG. Two of our new mission statements are to make great products that contribute positively to the world and steward sustainable manufacturing and operations practices to minimize environmental impact. While this has always been an important topic to us, we are accelerating our pace of positive change in this area.

On the environment side, our facilities meet world-class standards and are very focused on driving sustainable improvement. On the social side, we're great stewards in the communities where we work and are also very focused on the diversity of our workforce. So for example, 40% of our global workforce are women. And of course, as you all know, that makes me very happy. In the last year, we have overhauled our governance focus, and today we're world-class in everything, from board governance practices to ethics and compliance frameworks across our global footprint. We have lots to be proud of here.

So looking forward, my key message that I want you to walk away with today is that our growth strategy will be very focused in areas where we can win and differentiate, our new operational model is unique and will drive productivity and growth. The Flex business system will drive repeatable and consistent performance. Around all of this, we have wrapped a new organizational design and an incentive structure. Our strategy will lead us to change our industry and at the same time will put us in the top quartile of our performance range.

So we've developed a strategic framework that we're deploying in four areas. This framework will drive growth, efficiency, differentiation and consistency, and I'm going to run through each one of these. So as we looked at our business, we defined six primary end markets. The great news is that our markets are tied to strong secular trends like autonomous, clean energy, connectivity and digital healthcare. We also refocused each market-facing business group to be highly targeted in the submarkets they will prioritize. As you are aware, the available markets are very sizable.

So being clear in where we grow and enabling that with the right go-to-market and technology competency is critical to our future. For us, these are largely white space opportunities. These are big markets with plenty of room to play, not the zero sum battles you've seen in the past. So for example, let me talk in our health solutions business and give you an idea of what I'm talking about. The available market here is greater than $150 billion. We are only targeting areas where we have technology value propositions for the customer. In the medical device area of that market, we're interested in areas like personal diagnostics, surgical instruments, but we're not going to pursue submarkets such as cardiac implants. Furthermore, we'll accelerate our investments in areas like continuous glucose monitoring or portable monitoring devices where we can clearly provide value for our customers. This kind of disciplined growth framework is what we're deploying in all business groups.

And in addition to all of this, we have also reorganized our market-facing organizations. They will have end-to-end ownership for their respective businesses. I am a huge fan of simpler organizational models that drive speed, efficiency and, most importantly, clear accountability. Now combining this structure with well-defined hurdle rates will deliver our desired end state.

So the six end markets or business groups will be CEC, our communications, enterprise and cloud business, lifestyle, consumer devices, industrial, automotive, and health solutions. The key to success here is that each of these target end markets are distinct and they require a focus strategy with end-to-end customer value chain ownership, from finding the right high-value opportunities, driving execution to top performer status, and then leveraging that success to expand our position.

So what's the next piece in this long-term strategy? We need to find an operational model to support these segment-specific strategies and deliver the highest quality in the most efficient way based on the needs of our customers. We believe this new alignment will drive a strong emphasis on optimizing our footprint as well as capital in the most efficient way. As we think about these six end markets, in most cases, they naturally align along attributes that match up with our customers' value equation. What I mean by that is quality is always important. But for some customers because of the competitive landscape, that equation leans more to fastest time to market and best cost to value balance. Some customers require very specialized or regional productions and supply chains and, of course, for some, the cost of failure is so high that it eclipses every other factor.

So to execute this differentiated operational model that takes advantage of our scale but at the same time builds on our uniqueness, we will be reorganizing and optimizing our operations models along two separate reporting segments, streamlining for maximum efficiencies, leverage and simplicity. We are calling these two segments Flex Agility Solutions and Flex Reliability Solutions. We will start reporting our results by these two segments in fiscal year 2021.

So the Flex Agility Solutions segment is optimized for speed to market at any volume based on a highly flexible supply and manufacturing system. A very cost efficient cost structure and it supports relatively shorter product life cycles. And the Reliability Solutions segment is optimized for longer product lifecycles requiring complex ramps at any volume with specialized production models and critical environments.

I believe these two models will create a more dynamic and durable system. It will play to our strengths. It'll simplify our cost structures, particularly focusing on controlling what we can. The two models will position us to pivot faster where we need to, and deliver long critical elements necessary to grow in our end markets. In a few minutes, I'll have our two segment leaders Doug and Paul brief you on some of the characteristics of these groups and how we're optimizing and continuing to shift our mix to higher value businesses. And later Chris will talk you through the segment reporting. But before we get to that, I want to talk to you about how we are sharpening our differentiation. Our engineering teams have clear industry expertise and well-defined roadmaps that are focused on the highly selective domains we invest in. Integrated into our new defined segment groups, they will be aligned and fast in how they execute.

But in the long run we'll differentiate and redefine the categories we operate in. The short answer is that there is no one thing that accomplishes all of this, but how we create a unique combination of technologies, service and synergies and how we apply this combination to the markets we go after. The right target markets for us are the ones where our combination can lead to higher value relationship, which means taking a more active role in solving our customers' complexity. We believe our full stack of capabilities makes us truly differentiated partner. As the product ideas in these evolving markets become more complex, integrating more features and technologies is required. Customers are looking for partners who have the advanced design and engineering capabilities to help turn these ideas into manufacturable products. Additionally, you also must have a deep understanding of the industry specific applications.

There is no one size fits all solutions in these segments. We must have specific domain expertise to apply to your customers' challenges. This is where we can win differently from others. So let me talk through one example that I think ties this together. Think about our homegrown battery backup module for data centers that was developed by our industrial business and then is also deployed in other industrial businesses. As the world moves from traditional backup system to battery backup systems, we can combine this capability with our in-house developed battery management system technology and offer it to our automotive electrification platform. This shows us taking the new and disruptive technologies and creating synergies by applying them to a number of our core markets. Now that's a kind of differentiation and growth that excites me.

Finally, all of this leads to more complicated manufacturing requirements. We are redoubling our investments in futuristic manufacturing technology so our customers can lean on us for true differentiation from this investment. The last part of our strategic framework is the newly launched Flex Business System. I believe consistency is key to any good company. Our work last year has shown that driving common practices is not only great for productivity, but also makes us a more reliable partner to all our stakeholders. We are allocating committed resources and leadership to drive this part of our strategy. So we're targeting five key areas in the Flex Business System, and I'll just pick one as an example and talk through it. So think about the planning area, one of the biggest drivers that adds to supply chain whipsaw and added working capital inefficiency, and it's mainly due to poor planning processes by us, our suppliers and our customers.

We believe, we have developed a new playbook to rethink the planning activity for the whole value chain, and we are in the process of actively deploying this. Done right, this will improve our performance and at the same time minimize working capital exposure across the value chain. So we are using our new strategic framework to embark on our journey. Along with this, we have changed our vision, our mission and our purpose to align to our long-term aspirations. We have also changed our organizational structure to drive speed, efficiency and accountability. But most importantly, we have totally revamped our incentive plan to align pay for performance. And supporting all of this with reinvigorating our culture to drive collaboration, integrity and discipline, I believe is a powerful combination. So our teams are aligned and excited about how we're changing the industry and the landscape. I'm not saying that this is easy and I believe our transformation has just started.

Our aspirations for our results in the three-year window is as follows. We expect revenue to be higher than GDP as we grow and change the mix of the business. We're targeting mid single-digit adjusted operating margin with a 10%-plus adjusted EPS growth through the cycle. We will also be consistent and having 80%-plus adjusted free cash flow conversion, and most importantly combining all of those with the capital allocation plan that is balanced between investing in the businesses and providing shareholder return. Our strategic framework, as we have presented today, will drive our financial aspirations, and we are already seeing the results. Now, since we've reduced the time of this meeting, we'll do a very short update from Doug and Paul to describe some thinking around our segments.

In the Flex Agility Solutions, we will be disciplined in going after markets that match our platform, meet or exceed our margin and ROIC targets, and where we can truly add value to the customer. We still need to be prudent in some of these markets because competitive dynamics and other factors mean that the key to winning here is having the right operational model that can efficiently deliver quality outcomes, benefit from scale and drive the most leverage in the system. This is our thinking for Flex Agility Solutions.

With that, Doug Britt is going to talk more about this business.

Douglas Britt

President-Integrated Solutions, Flex Ltd.

Thank you, Revathi. Hello, everyone and thanks for participating on today's call. Our Agility Solutions segment consists of lifestyle, our CEC business, which is communications, enterprise and cloud and consumer devices. Lifestyle is a combination of our home and lifestyle business that was contained within IEI, and our consumer packaging that was previously a part of CTG. Our consumer devices business contains mobile, laptops, PCs and other high velocity consumer device customers. Our Agility Solutions customers tend to have shorter product lifecycles that require a highly flexible supply chain and global manufacturing system with world-class quality. We deliver value through end-to-end supply chain services, and we optimize for any volume, mass customization and efficient cost structures.

Flex Agility differentiates through design, vertical integration, regional manufacturing and aftermarket services. We have strong design capabilities in cosmetic plastics, racks and enclosures, compute, storage and communications. These capabilities are often leveraged across our health solutions, industrial and automotive businesses for new applications. One example of this is when our automotive team leveraged our CEC, compute and communications design expertise to win several major autonomous programs over the past two years. This has been a differentiating factor in securing these wins. Our global footprint and agile delivery model promote flexibility and industry-leading quality performance, enabling us to be hyper responsive to our customers' needs.

A recent example of our operational agility was our response to a supply chain disruption caused by the COVID-19 outbreak. One of our major CEC customer's supply chain from Asia to Europe was disrupted due to the abrupt closure of one of our European fulfillment centers. This center is located within an effected region. As part of our continuity plan, we immediately shifted this fulfillment operation to an alternative center within our European network and resumed fulfilling orders within 24 hours. Flex Agility has frequently been recognized for our supply chain service innovation. We recently won five supplier awards from Cisco, including Supplier of the Year Award. We have the broadest service offering in the industry, and when bundled, build strong customer affinity.

Flex Agility is well-positioned to continue to deliver solid free cash flow and ROIC for Flex. Our Lifestyle segment is addressing a massive TAM, but not all of it is a fit for Flex. We have defined five targeted markets mostly comprised of durable electronic goods with a high degree of complex mechanical content. We're focused at winning with the market leaders in each of these categories. Those markets and accounts are tightly aligned with our strategy to provide customers with enabling technologies in connectivity, mechanicals and human machine interface to bundle multiple services in the same opportunity and execute within our focused global footprint. Our strategic objective is simply to help our customers to get to market faster, move reliably and more cost effectively than they could otherwise do on their own.

Our strategy is working as we have benefited from multiple years of strong bookings. Year-to-date we've closed $700 million in new bookings will set us for continued growth in fiscal year 2021. We win in a market by packaging the Flex platform of capabilities into a differentiated solution that responds to unique challenges faced by lifestyle companies, which are always seeking ways to differentiate the look of their products while creating a richer customer experience. Connected devices will gradually automate all aspects of the home. Hardware companies are constantly redesigning their traditional products into smart products on isolated design tools that don't easily transition into mass production. We have developed a human machine interface platform to enhance user interaction through touch, motion and voice.

We also deliver high-end cosmetic enclosures in all key regions of the world leveraging our design-led tooling capabilities and global footprint. Our connectivity developer kit enables companies to quickly innovate on a design platform that is already integrated with the Flex manufacturing and supply chain network. What really differentiates lifestyle is the breadth of our design and service offering and how we uniquely bundle them into each opportunity. This approach places Flex ahead of our competitors, increases the value we provide to our customers and results in wins at higher margins. This example illustrates our approach is working to win in the market. We recently won a next generation cordless vacuum with a leading consumer brand.

We create an end-to-end vertically integrated solution. We build all the electronics, we build the battery packs, we design all the tools for all the plastic parts, we manufacture all the plastic parts and we assemble the complete product. In this case instead of providing one service with one source of margin to simply assemble the vacuum cleaner will provide five services with five sources of margin into the same opportunity. We will continue to expand our customer base and add value through our differentiated service offering. Lifestyle will continue to be a growth engine for Flex Agility. In our CEC segment we are focused on winning within the data center, edge and communication infrastructure markets.

This segment provides significant scale to Flex, and we get access to leading edge technology that can be leveraged across all Flex businesses, whether it's driving our compute and communications technologies into new use cases across automotive, industrial and lifestyle, or providing continuous scale of business to keep our factories highly utilized. CEC is critical to the success of Flex. This strategy for CEC is to sustain our strong relationships with our existing customer base and expand engagements with new targeted customers. Our leadership team has deep technical experience, and we continue to build upon strong communications, data center and converged infrastructure competencies to win more design-led programs. Our new bookings to-date have reach 1.6 billion. Our customer diversification strategy is working as we've added 15 new customers this year. This provides CEC a solid foundation to return to growth.

In CEC, we have four major pillars of differentiation. The first is speed the market. We have expertise providing design and design support to launch new products, and ramp complex supply chains within any key region of the world. We have developed a portfolio of reference architectures based on next-generation silicon technologies to reduce design time. Second, our global and regionalized footprint allows us to ensure business continuity. Our customers rely on our ability to adjust our supply chain to meet market dynamics, and optimize for costs, quality and delivery lead time. Our regional manufacturing solutions are valuable as we continue to help our customers optimize our supply chains to address the fast changing tariff and trade environment.

A third pillar is operational excellence. We develop automated manufacturing solutions, and are committed to drive continuous improvement through lean manufacturing and supply chain. And finally, technology. The heart of our technology leadership is our design competency in compute, storage, power management, mechanicals and communications. These capabilities provide increased value to our customers, and help them reduce time to market.

We're winning with several design-led projects in 4G and 5G radio, and base band deployments. We have designed with several spectrum alternatives as well as different mechanical form factors based on environmental requirements. These radios have been designed for automation, and can be deployed in one of our regional manufacturing facilities. At the core of these wins is the strong wireless design expertise in our Finland Design Center.

Our consumer device business is the combination of mobile, laptops, PCs, and several high-velocity consumer device accounts. This business provides Flex with material supply leverage that helps competitiveness across our other segments as well as leading manufacturing process technology. We will defend and protect our relationships with our customers that deliver solid free cash flow and ROIC, and we will manage very selective in our customer engagements in this business, and we're committed to manage the mix of this business ongoing. It is our expectation that we will have a year-over-year decline in fiscal year 2020 run revenues as we see the impacts of our customer exits as we continue to manage engagements that don't meet our financial thresholds.

In summary, Flex Agility differentiates through a broad end-to-end service offering, which includes design, vertical integration, regional manufacturing, and aftermarket services. We also deliver value through optimization for any volume, mass customization and efficient cost structures. We will deploy the same commercial and operational discipline that we used to deliver solid results in IEI over the past seven years. This commercial and operational discipline coupled with our expanding value-add offerings position us to expand margins.

Our consumer devices business will see declines in the range of a $0.5 billion, but this will be offset by healthy growth in revenue for both CEC and lifestyle. We will increase customer affinity through our broad service offering, our regional manufacturing footprint, and meeting and exceeding the quality and delivery expectations of our customers. Thank you.

Revathi Advaithi

Chief Executive Officer & Director, Flex Ltd.

Okay. So, you just heard about how our Agility group has a clear view of where we want to bundle and grow, but only within an operating model that supports stringent ROIC and cash generation hurdles. You also heard that the Agility group provides scale and technology knowhow creating synergies that benefit the entire organization. We believe we have the right formula of providing differentiated technology combining with delivering solutions at speed that give us a competitive advantage in the agility market.

So now, moving to the Flex Reliability Group. We've had a good history of moving up from the EMS businesses to join design and development to full product development in some of our businesses. Doing that in a structured way moving forward will be the core principle of this group. We will target engineering capability very clearly to build differentiation, and make sure we're selling this value to customers.

With that, I'd like to turn this over to Paul Humphreys to talk about our Reliability group.

Paul J. Humphries

President-High Reliability Solutions, Flex Ltd.

Thanks, Revathi. Good morning, ladies and gentlemen. I'm pleased to have the chance to talk to you this morning about our Flex Reliability Solutions. Reliability Solutions now consists of three groups: automotive, health solutions and industrial. All three segments have similar characteristics that I will expand on in the next slide. We believe the strategy and playbook that we initially developed for automotive, and subsequently adopted for health solutions, is equally applicable to the industrial segment which can help further drive revenue and margin growth. This includes a leadership team with deep industry and domain expertise, a growth strategy focused on areas of the market that are supported by long-term secular trends with above average market revenue and margin growth, and a broad-based design, technology and manufacturing platform, combined with the reliable solutions-oriented business model.

As I referenced in the previous slide, the three segments have many similar characteristics. All three segments are undergoing significant market and technology shifts, and all include complex, high-technology products with exacting quality and regulatory standards, but have long design and product life cycles. These characteristics provide significant opportunity for revenue and margin growth, but demand solutions focus business model that can support our customers' needs to accelerate change while still ensuring we provide the highest levels of quality, reliability and compliance.

Currently, the global automotive market is flat to down. We're still very excited by the long-term megatrends in this industry. We see the drive towards zero accidents, zero emissions, mobility services and seamless connectivity continuing to accelerate, and our strategy to focus on autonomy, connectivity, electrification and smart-tech has us very well-positioned. Over the past few years, we have built our global automotive design and manufacturing competence in these areas, while simultaneously leveraging across industry expertise in compute, power and consumer electronics. As a result, we've been able to develop cutting-edge products for our traditional OEMs and Tier 1s as well as new emerging mobility players.

By developing this differentiated offering and continuing to invest towards market trends and emerging technologies, we have emerged as one of the new global industry disruptors as recognized by IHS Markit, an industry-leading research an information provider. This has been reflected in the significant new bookings we have secured this year, and we are continuing to increase the content we supply per vehicle as well as expanding our presence across an even broader range of global vehicle nameplates. We are confident that our strategy is working, and we will continue to see above average industry growth as we further build our reputation as a credible alternative to the traditional Tier 1 supply base.

As we have stated throughout this presentation, we are still confident we have a highly regarded and differentiated model that is recognized by customers and industry sources alike. Our technology-focused solutions driven strategy differentiates us from both our Tier 1 and traditional EMS competitors while still providing our customers with a competitive offering. This has been reflected in several customer and industry awards as well, as I mentioned previously, in record bookings. This is also brought out by the fact that we are now ranked in the top 100 global suppliers by Automotive News. We are confident that our established and growing reputation will only lead to further wins.

A great example where we have leveraged the expertise of our design teams is in the development of a 48-volt DC-DC converter that has proven to be a major success for mild hybrid vehicles in the electrification space. We are now launching the third generation of this product for a European OEM. Our design has unique performance features not available from any other supplier while still providing the customer with a cost competitive solution.

Turning to health solutions. We have a segment that is a world leader in medical devices, medical equipment and drug delivery. The markets we have elected to play in have significant growth potential, and compound annual growth rate is above the average growth rate of the industry overall.

Within medical devices, where we support 85% of the top MedTech customers worldwide, we are the clear leaders in diabetes solutions and have a dominant position in medical disposables and surgical instruments.

Similarly, in medical equipment, we are leaders in life sciences, hospital-based patient diagnostics, and in imaging equipment. While in drug delivery, we support 18 of the top 20 global pharma companies with drug delivery devices for biologic drugs.

Like automotive, we started in this segment with low complexity EMS business, but over time have built domain expertise in design, manufacturing and quality across our focused areas that have enabled us to provide differentiated solutions that no one can match in terms of technology competence or ability to scale. We are confident that with continued investment in these core areas, we can sustain long-term growth rates that exceed the industry average.

Flex has a 30-year history of supplying world-class levels of quality and reliability. This combined with our deep domain expertise in design, new product introduction and manufacturing of medical products has served to support our health solutions customers' needs globally. This has positioned us as a reliable credible partner, who can meet the most exacting product and regulatory standards with vertically integrated technology driven solutions. This has been rewarded not just in the increased bookings we've experienced, but also in the recognition we receive from customers and industry sources.

A great example of this is a continuous glucose monitor that we are ramping in our Buffalo Grove facility. This is a product where we offer the customer the most vertically integrated manufacturing solution comprising plastic injection molding, electronics manufacturing, fully automated assembly, sterilization, and automated packaging, all out of one site. Design life cycles and ramps are long in this industry, sometimes exceeding five years. Facility buildouts, product qualifications, and regulatory approvals create a long ramp and take time. But however, they lead to large lifetime revenue opportunities often in excess of 10 years.

At the 2018 Investor Day, we showed you the timeline for the continuous glucose monitoring business in Buffalo Grove that you're looking at today. Well, it's now 2020, and we're on track. In fact, we were able to pull the initial launch date ahead by a few months, and are now ramping up for full scale production in FY 2021.

Our execution performance has also led to additional wins. We have been awarded the next generation of an advanced diabetes management product for a leader in diabetes care. This is just one example. There are also others in the pipeline that we're similarly excited about.

Our industrial segment is addressing a massive TAM, and has started to focus on those opportunities that play to our strengths and where we can provide a differentiated offering. Just like automotive and health solutions, customer engagements often start with EMS opportunities, but we are already moving up the stack by providing engineered solutions in mechanicals technology, connectivity, actuators and embedded power. We are also leveraging the broad base capability that Flex has available in value engineering, across a broad range of product categories where we can offer customers differentiated value-based solutions. Year-to-date, we have secured in excess of $1.2 billion in new bookings with 69 new targeted customers, which positions us for continued growth in FY 2021.

Our industrial business has been on a strong growth trajectory for several years. Our ability to support the scaling of large complex systems in any region of the world has provided an excellent platform for growth. Following a playbook that is very similar to automotive and medical, where we often start with EMS opportunities, industrial is moving up the stack with comprehensive design, engineering and manufacturing solutions. As a result, we've been able to secure new wins in dispensing systems, actuator systems, power, battery management and robotics that have helped to win against the competition. We are confident that this differentiated model will help to drive continued growth across our entire industrial segment. While it's still early for us in some parts of the industrial space, our playbook is working, and we are moving up the value chain.

One example is an advanced data center battery backup solution. This was a design-led win based on our Flex battery management system IP portfolio. So, this leverages capabilities both in our industrial segment in lithium-ion chemistry and power management as well as expertise from our CEC segment in data center applications. This solution is currently deployed with a large industrial customer, and we have several more wins that we're closing on currently.

To summarize, these are our commitments for Flex Reliability Solutions. We will leverage our domain expertise to increase design-led engagements leading to a better mix of higher value wins in our portfolio. Simultaneously, we'll continue to stay ahead of the technology curve, and enhance our technology capabilities in preparation for the future. Where it makes sense, we'll continue to leverage the synergies from other business groups such as we have done to-date for power, cloud compute and autonomous vehicles. Lastly, I'm committed to expanding margins generating industry-leading growth across all the markets that we operate in. Thank you.

Revathi Advaithi

Chief Executive Officer & Director, Flex Ltd.

Thank you, Paul. The reliability playbook will be focused on technology-driven growth. As he said, we have unique and differentiated engineering-led solutions that'll drive the growth for this segment.

Now I want to turn it over to Chris Collier to talk about our financial framework. Chris?

Christopher E. Collier

Chief Financial Officer, Flex Ltd.

Thank you, Revathi. The Flex management team appreciates your time and attention today. Over the past 12 months, we've been very busy. We've been refining and improving our portfolio, refining and improving our business processes, refining and improving our operational and organizational structures. We continue to make progress tracking to our strategic goals of margin expansion, earnings growth, strong cash flow generation, and shareholder value creation. And so, I want to continue our discussion today and share some insight on our recent performance, our disciplined execution as well as changes in our operating model and long-term financial framework.

I think a great starting point is to look at our improving performance across a number of metrics. What we are showing here is our financial performance on a last 12-month basis compared to the prior two fiscal years. When I say last 12 months, this takes into account the 12 months ending our last earnings, which was our Q3 of fiscal 2020. Despite multiple factors beyond our control, we're very pleased with our financial performance and ability to deliver on our commitments.

When looking at our revenue and noting the decline, this is a distinct reflection of our elected actions taken to improve our portfolio, and to truly manage our mix. We continue to improve our operational execution, and we are operating with greater discipline, which when combined with our better portfolio mix has led to greater adjusted operating income and expanding margins. And this improved profitability flows through to the strong adjusted EPS growth. Our improved earnings coupled with our disciplined capital management has positioned us back to delivering solid cash generation. So what this does is provide us a strong foundation to be driving from.

We are making progress towards stabilizing our financial performance. There are clearly certain elements to highlight in this progress such as our disengagement from over $1.2 billion of low margin, high volatility businesses as well as our focused efforts to continue to tilt our portfolio to growing businesses, including industrial, automotive and health solutions. You also have seen strong adjusted gross and operating margin improvements as we have maintained a very strong cost discipline. We recognize that we've been managing this transformation through a dynamic geopolitical and challenging tariff and trade environment.

Now I think it's really important to consider the diversification resulting from our portfolio management actions. Overall, we're operating a well-diversified portfolio, one that is diversified across markets, across countries and customers. I'd like to emphasize that we have been focused on repositioning ourselves globally to address the ever changing regionalization needs of our customers, and this has resulted in a nicely balanced regional footprint. Our global system now has our Americas region hosting more of our installed PP&E than any other region. We also expect our Americas region will end 2020 as our highest revenue generating region, a first in the history of Flex. In the chart on the left, you can see we have no single product market that is greater than 15% of our sales, and we are really pleased with our continued expansion and increased concentration of long cycle businesses in our portfolio. Overall, we believe this diversified portfolio is valuable, and provides for a more sustainable and profitable business.

Improving our gross margin is a focal point. We've improved our adjusted gross margin for the past three quarters, and in fact we hit 7.1% just last quarter. This is not only a reflection of focused efforts on our portfolio mix, but also with our improved operational execution and discipline. Our portfolio is capturing more design and engineering content as well as more value-add in our services, which aides greater gross margin. As you had heard earlier, Revathi has reinvigorated and amplified our focus on multiple operational elements and business excellence, and these efforts are reflected in operational efficiency and productivity improvements. We have distinct actions and initiatives that our teams are driving that have resulted in improvements to our demand planning, our sales and operational planning, and even through renewed emphasis and efforts on Lean and Six Sigma. Our teams are taking action on our operating cost structures to improve our efficiency and anticipate further capacity utilization benefits as we operationally structure around our delivery models. Overall, we're – we have clear objectives to deliver adjusted gross margin improvements to over 7.5%.

We do a great job of managing our SG&A with discipline, and we are truly driving industry-leading SG&A expense management. We have a relentless cost focus, and we've been taking distinct and direct actions to drive better efficiency and productivity across the enterprise. The key area where we've been vigilant has been our R&D and innovation spend, which is contained within our SG&A. While this spend is very important to our future, we've been thoughtfully repositioning our design and engineering offering, and overall more discerning and focused on optimizing our spend. We continue to align our design and engineering, and innovation investments with clear go-to-market strategies and target product categories. We now better leverage our capabilities and capacity across our entire company. We remain confident in our ability to operate in the range of 3% to 3.2% of revenues, and support our future growth. And this creates meaningful earnings leverage.

From this chart, you can see significant reduction in fiscal 2020 capital investment, which is due to our increased discipline as well as we are benefiting from repositioning and redeploying assets throughout our system in an efficient way.

It's important to note that we have invested at meaningful levels in the recent years, and possess a well-built-out system for both capabilities and capacity. We've increased our rigor and discipline related to our assessments and approvals for capital investments, and have truly focused our investments in our core growth areas.

While we target our CapEx investments to fit within depreciation levels, we are confident that we are adequately investing into the core areas of growth, and we are putting meaningful investments to support our future growth in automotive, health solutions and industrial as well as automation for our entire global operations.

Cash flow generation is a key element of our business model. You can see from the chart that in the last 12 months we've been able to return to strong cash flow generation. We've been able to return to solid cash generation by managing our net working capital nicely in our targeted range of 6% to 8% of revenues and through the disciplined capital investment that I just talked about, and lastly coupled with our improved earnings. So, we believe that we are structurally positioned, and fundamentally operating our business to deliver our adjusted free [indiscernible] (00:57:35), and we are committed to doing so.

Now when you look at our capital structure, you see that it's well-balanced and very flexible, and that is by design. We are investment grade rated. We have staggered debt maturities with no meaningful near-term maturities, and none that exceed our expected annual free cash flow.

We have a low average cost of debt, and we have a good mix of fixed rate and floating rate debt, which as a result of the current rate environment should benefit us. We have ample liquidity to our cash position and our unused revolver. So overall, we're really pleased with the structure we are operating. We're well-positioned to support our current and prospective business, and it remains our objective to operate with a strong financial flexibility.

The underlying premise of our capital allocation methodology is to create shareholder value with a long-term commitment. The two key aspects we balance in our capital allocation are investing in the business and providing shareholder returns. We believe we are well-positioned and have tremendous opportunities in front of us, so we'll continue to focus on our business. This is primarily through investing organically in the business to grow and deliver solid ROIC. We'll be very targeted in M&A, and as such it will be limited as we possess well-built-out global system with solid capabilities to support core target growth markets and the megatrends.

And so, M&A investments will be tilted to our long cycle businesses in growth segments. Operating with a balanced and flexible financial condition that remains investment grade rated is a core to our strategy. It is our distinct objective to repurchase stock to offset share dilution and to provide shareholder return. Share repurchasing has been and will continue to be a key feature of our capital allocation strategy. And in particular, we want to clearly state that we will be opportunistically be a purchaser of our shares, and that our fiscal 2021 repurchasing will increase. The bottom line is that we will be driving disciplined capital return through returning our free cash flow to our investors, while sustaining our sound financial condition.

As presented earlier by Revathi, effective in the first quarter of fiscal 2021, we will reorganize our operating structure into two new reportable segments to better align with our go-to-market strategy and capital allocation priorities. We have Flex Agility Solutions, whose primary business groups include consumer devices, lifestyle and CEC. And there is Flex Reliability Solutions, whose primary business groups include automotive, health solutions and industrial. We see multiple operational and commercial benefits from this structure. Most notably, we anticipate better alignment between our volume and mix variables within our delivery model.

We anticipate better capacity utilization, improved capital deployment, and more efficient management of ramping businesses. And from a commercial lens, we see improved alignment with our go-to-market strategies. We also see the ability to drive more efficient and deeper sales coverage across the various markets we serve. So, as a result of this transformation, we expect to achieve gross margin expansion, better operating expense leverage and improved profitability and ROIC.

Here we want to provide you with some insight into the Reliability Solutions segment. On the left, you have a LTM snapshot, so you can understand the relative size of revenue, earnings and its adjusted operating margin. In the middle, you see a breakdown of sales by the underlying business units, with the largest being industrial, followed by automotive and then health solutions. In Reliability Solutions, we have a high mix, higher margin business with longer underlying product life cycles, and higher capital intensity, but strong anticipated growth. As Paul highlighted earlier, we're very well-positioned with a deep domain expertise, a strong global scale, and a wide breadth of products and capabilities. In addition, we are able to lead our engagements through our design and engineering expertise. Our expectations for this business is to have solid growth prospects, and to continue to expand its margin, based on the greater levels of value-added services it continues to book.

Now turning to our Agility Solutions segment. Here on the left side, we're providing an LTM snapshot again highlighting the revenue, operating profit and margin profile of the business. In the middle, you see a breakdown of sales by the underlying business units with the largest being our CEC business, followed by lifestyle, and then consumer devices. This business segment has a higher variability in its revenue, and a lower mix of products, and the underlying product life cycles is shorter, and in the range of one to four years. In this business, we are focused intently on its fixed and variable cost structure as well as higher capacity utilization and lower capital intensity as we look to be optimizing for the variability of its revenues.

As Doug highlighted earlier, we have some real differentiated capabilities and strong partnerships, which are enabling us to have some solid underlying profitable growth opportunities while we continue to be thoughtful about which product categories and partners we engage with. Our expectations are for this business group to grow, but more GDP like as it's not focused on growth, but rather our goal is for it to expand its margin based on the greater levels of value-added services it continues to book, and for it to be highly capital efficient.

Putting it all together, we believe that we are structurally and fundamentally positioned to deliver our long-term financial framework. And we're excited about the future potential of the business. In terms of revenue growth, we expect to grow organically at or above GDP, and continue tilting our portfolio mix focus to longer-cycle businesses. We have clear efforts for earnings expansion, where we're driving to mid-single digits operating margin, and a 10%-plus annual adjusted EPS growth.

Our business model provides strong cash generation through our earnings expansion and disciplined investment levels where our objective is to deliver an 80%-plus free cash flow conversion. And our framework provides that we are prudent stewards of capital, which see us maintaining our investment grade rating and increasing shareholder returns.

In closing, we are focused on our business systems, processes and discipline to guide our decisions and actions that will enable us to deliver long-term shareholder value, and a solid sustainable business that you can depend on.

Now I'd like to turn the call back to Revathi for some final remarks before Q&A.

Revathi Advaithi

Chief Executive Officer & Director, Flex Ltd.

Okay. Thank you, Chris. So, as I said before, what we want you to walk away with today is that our growth strategy will be very focused in areas where we can win and differentiate. Our new operational model is unique, and will drive productivity and growth. The Flex Business System will drive repeatable and consistent performance. Around all of this, we have wrapped a new organizational design and a comprehensive incentive structure. Our strategy will drive us to lead and change our industry, and at the same time put us in the top quartile of the performance range. This is the first of many conversations I will have with all of you on our new direction. I'm excited about this path, and this new drumbeat we're marching to and we're confident that this will deliver the right results for all our stakeholders.

Now I'd like to turn this back to Christine to start our Q&A session.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Your first question comes from the line of Matt Sheerin from Stifel. Your line is open.

Matthew John Sheerin
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Yes. Thank you very much. Just first question, Revathi, regarding your margin targets of mid-single digits. It would be great if you could be a little bit more specific are we talking 4% to 5% range, and is there a timeframe around that?

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

Hey, Matt. Thank you for the question. Our whole thinking around all the strategic planning was in the one- to three-year framework, and that's our thinking around the timeline. In terms of kind of what exactly mid-single digits, I'm going to leave that range open where we are positioned, and how we have aggressively improved the margins through the last few quarters. So, I'm assuming that we will start moving towards the 4-plus-percent range pretty quickly here in the next year, pending all these coronavirus issues, and then aggressively move forward from that.

Matthew John Sheerin
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Okay. Great. And then, as my follow-up regarding the Agility business and specifically the mobile devices where you have been pruning the portfolio, how much is left there? And could you give us an example of a program that's working, and one that may not have worked, and what the difference is? And are you seeing customers being receptive at all to changing the metrics in terms of those agreements, so that it'd be more profitable or longer-term engagements for you?

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

Okay. Matt, hey, thank you for the question. Let me first step back and just talk to you about mix and pruning as you discussed. I'll just tell you this. My view in general is that every segment and every business group has a portfolio of products, and their continuous work is to move that portfolio of products up towards our hurdle rates, which means that within every segment they will continue to manage mix and make sure that they're selling value. That wouldn't apply just to our consumer device segment, that'll apply to all our segments. So, I just want to make sure that we're clear in terms of my view on kind of improving mix and shifting mix in the right direction.

That being said, on the mobile – on the consumer device side, it clearly is a portfolio where we see that how we manage and deliver this operational model that we're deploying is important, right, because those customers do tend to have very short life cycles of products, they're moving up and down their production pretty quickly as they go through these production life cycles, so we have to be really optimized for kind of large volumes, and have a very efficient and flexible cost structure. So, that's kind of how I see kind of the whole consumer device segment play through. And some of this is going to be whether customers are accepting of what we are trying to propose in terms of the delivery model, and some of it is going to be our own willingness to accept the risk-adjusted ROICs of that business.

So, I'll tell you in terms of a program, let me give you an example just in terms of Flex Agility and where program is working and where it isn't, right. Just where it's working, this is not related to consumer devices, but related to CEC. If you think about the last year, in the middle of Q2 of last year, we saw a significant decline in our CEC volumes, and all you guys who have followed this portfolio for a long time know that some of the customers in our Agility portfolio tend to scale up and down pretty quickly. So, when we saw that shift and the change in Q2, we had to take some pretty aggressive actions in a short amount of time, and we were able to do that and bring back our Q3 margin performance back in line to where we needed it to be.

So, our general view is that if we have the right fixed and variable cost structure for our Agility customers right down to all our factories and our product lines, then we will be able to manage these shifts in a more optimal way for our customers and ourselves. And that would be an example of where I'll tell you that we saw the effectivity of it, and now we're kind of memorializing that in our operating structure, so we will make sure that our plants can really run with that type of thinking in place.

Matthew John Sheerin
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Okay. Thank you very much.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

Thank you, Matt.

Operator: Your next question comes from the line of Jim Suva from Citi. Your line is open.

Jim Suva
Analyst, Citigroup Global Markets, Inc.

Q

Thank you very much. And I have two questions, I'll just give them to you right now, and you can take them in any order that you prefer. I believe during your prepared comments, I can't remember if it was the comments prepared by CFO or CEO about a disengagement of like $1.2 billion of low margin business. Can you remind us, is that what you have already done or in the process of doing or have yet to do?

And then my second question is probably I assume more of a strategy, a bit CEO question, but maybe also CFO is, in the past Flex has been in consumer devices really big, then kind of scaled back, and in vertical very big, then scaled back. Can you help us understand kind of what's different this time about the consumer devices and vertical integration? Thank you.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

Jim, I'm going to give both those questions to Chris, he is in a great position to talk to about history and what we're doing differently and the $1.2 billion. So, Chris?

Christopher E. Collier
Chief Financial Officer, Flex Ltd.
A

Yeah, for sure. So Jim, one of the slides that I showed was the progress we've been making to drive stabilization and improvement in our business. That slide where you're noting the $1.2 billion is what was accomplished in the last 12 months. If you look back to last July on our earnings call, we'd highlighted that we took distinct and direct actions to resize and direct our portfolio differently. And that resulted in over $1.2 billion of highly volatile, low margin business being exited by the company. You also heard Doug say that still as we step into next year, we have about a $0.5 billion of an overhang that continues.

All this is as a result of our distinct efforts to be focused on the mix of the business we're operating. We've been really focused in 12 months, have been very consistent in terms of what consumer devices and programs that we would partner with. We had highlighted in the front end of the conversation the new and changing efforts to run our business excellence in our business systems. That stems from contracts to pricing to how we launch businesses. All that is centered around establishing clear hurdle rates and payback periods and returns in terms of where we're engaging with that business.

So hopefully, that kind of gives you a bit of background in terms of what happened in that device piece over this past year, and how we think about operating it with due care and thoughtful discipline moving forward.

Jim Suva
Analyst, Citigroup Global Markets, Inc.
Q

Got you, Chris.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.
A

Okay. Thanks, Jim.

Jim Suva
Analyst, Citigroup Global Markets, Inc.
Q

So, if I got it right, then the disengagement of $1.2 billion is behind us, but looking forward you have about $500 million yet to disengage if I got the numbers right.

Christopher E. Collier
Chief Financial Officer, Flex Ltd.
A

On a year-over-year basis, we will be down in that group by around $500 million.

Jim Suva
Analyst, Citigroup Global Markets, Inc.
Q

Got you. Thank you so much for the details. And by the way, good job at doing it virtual, one I fully support that given the health situation. Thank you.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.
A

Thank you, Jim.

Operator: Your next question comes from the line of Ruplu Bhattacharya from Bank of America. Your line is open.

Ruplu Bhattacharya
Analyst, Bank of America Merrill Lynch

Q

Hi. Thank you for taking my questions, and thanks for all the details today. Revathi, you gave a long-term revenue growth target of – which is an organic target at or above GDP. I was wondering if you can talk about your thoughts on M&A and inorganic growth. What are some of the things that you look for in targets, and given that the market valuations have pulled back, how should we think about inorganic growth on top of the organic growth target?

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

Okay. Great. Hey, Ruplu, thanks for that question. We were talking about organic growth as I talked about GDP plus is where we are targeting. And just a little bit more commentary on that is the way we should think about that is that our hope is for our Reliability Group to be growing above GDP, and then, our Agility Group will grow below GDP just because of the continued focus that we'll have and the right type of growth in that business.

In terms of M&A, yeah, valuations are subdued right now. The way I would think about it would be that we would look for good tuck-in acquisitions, particularly technology-focused tuck-in acquisitions that will be in – specifically focused around our Reliability segment or could be in areas like 5G if it helps solidify our position in there. But it has to be very technology engineering-focused acquisitions that really enhance our capability from where we are today. So, that's important to us. We are looking at that, and recasting our segments in a more clear way. And then, also having very clear alignment underneath those segments in terms of the subsegments we'll participate in, and will excel at, really provides a clear viewpoint of how we drive organic growth. But what types of acquisitions make sense. So, we have done a very thorough end-to-end look at this, and the current view here that we've given you is around organic, obviously M&A plays out as we find the right type of fit.

Ruplu Bhattacharya
Analyst, Bank of America Merrill Lynch

Q

Okay. Thanks for that Revathi. And just for my follow up, I wanted to talk about your manufacturing footprint. So you've laid out two different segments now, the Reliability segment is expected to grow faster than market, Agility Solutions more GDP, do you think given that kind of growth over the next couple of years, do you have the right manufacturing footprint? And do you think given everything happening in China, do you think you have to maybe adjust your manufacturing more out of China? So maybe just talk about your thoughts on where your factories are today, and any guidance on CapEx over the next couple of years. Thank you so much.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

Okay. Hey, thanks, Ruplu. One thing I'll say is, what's the beauty of our new operational model that we have laid out today is that we will have a very clear view of the types of factories and facilities that fit each of these models, and what type of capacity utilization, fixed variable costs we need to have across each of these models globally. And as we evaluate that and look at it, we do realize and understand that we have room for good optimization and productivity improvements across our footprint just because of this new focused view we are taking. So not only does this help in terms of consistency in the long-term, what it really does is drive very strong efficiency and productivity for us at the factory level, which does result in some footprint optimization that we will have globally. But that's a good thing because it's good look for productivity opportunities and be optimized in terms of our footprint.

I'd say globally we're fairly well situated. But one of the slides that Chris showed you is how our percent PP&E has moved across the regions, and how if you look right now he mentioned that our Americas region is one of our largest investment areas, and that's a result of all the supply chain shift that you've seen that has happened over the last 12 months, and that we think will continue to happen. And we have done a really effective job of managing that and you'll see that in our PP&E changes that have happened across the globe. And so we think we have been effective in that. We'll continue to be moving our footprint to suit the right supply chain strategies of our customers. But more importantly what I want all of you to walk away with this, that our new operational model delivers a factory optimization and a productivity improvement that we think drives our margin expansion also in the long run.

Ruplu Bhattacharya
Analyst, Bank of America Merrill Lynch

Q

Okay. Thanks for the details and thank you for taking my questions.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

Thanks, Ruplu.

Operator: Your next question comes from the line of Adam Tindle from Raymond James. Your line is open.

Adam Tindle
Analyst, Raymond James & Associates, Inc.

Q

Okay. Thanks and good afternoon. Revathi, I just wanted to start, you've got a lot of interesting goals that you outlined, but just wanted to double quick since we typically think of some of these as offsetting levers in the industry, and specifically you talked about wanting to return the company to organic revenue growth, typically requires CapEx to do that. You also want to grow in the high mix areas, usually requires more working capital, pure play, high mix companies like Plexus for example have cash cycles north of 3 times yours. But with the high mix growth acceleration you also talked about wanting to improve free cash flow conversion to over 80%. So the question, I guess, maybe what enables incremental growth in a high mix areas with lower working capital and CapEx, how you can keep SG&A flat during that, and why focus all of these pools concurrently?

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

Okay. Adam, that's a great question. So here's my view on that Adam, is that the reason why we think we can focus on these goals concurrently is because of the underlying assumption that we can improve our efficiencies in all of these areas. So for example, if you think about organic revenue, I've said this before that in this industry growth for the sake of growth is not exciting for me or for this business anymore. So we're going to be focused on the right kind of growth, which means that we'll continue to manage the portfolio and grow more aggressively in Reliability and grow more aggressively in the lifestyle business in Agility, and maybe manage the others more prudently. But in terms of so our mix driving to Reliability will change. What makes me think that we can manage all of these metrics at the same time is the fact that if you just think about capital investment for a second, we have tremendous room for doing this more efficiently than what we have done before.

So we're just very rigorous in terms of making sure that we're deploying capital with the right expectation in terms of ROIC and payback, we are being very good in terms of our governance model, and we're finding just improvements and efficiencies just because of asking the right questions as we are deploying our CapEx investment. So we think we have room to just do it more efficiently. And the same around free cash flow. I talked about doing our planning processes much better. I truly believe and we're seeing that that we should be improving our working capital if we deploy the right planning purposes for us and for our customers, it's going to improve working capital for all of us. That makes me think there is room to be better in terms of our free cash flow conversion even as we are shifting our mix. So those are all the underlying reasons, Adam, why we're making the statement that we can improve these metrics even as we are changing some of the characteristics in terms of where we grow and how we grow.

Adam Tindle
Analyst, Raymond James & Associates, Inc.
Q

Okay. That's helpful. And I also caught that you talked about changing incentive plans. I think you talked about pay for performance. I guess the question on that, what metrics are you looking for in performance and how pervasive is this, is it business leaders, sales teams, engineering teams?

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.
A

So Adam we've done a comprehensive review and a workout on our incentive plans across our organization. So it covers 80,000 employees across our organization. So it starts all the way from my team to everybody else in this organization. So it's very comprehensive. Pay for performance will be focused very clearly in terms of aligning with our shareholders. It starts with meeting our EPS metrics, and then goes down to meeting sub-metrics associated with meeting our EPS metrics. So it's very extensive, very comprehensive, and we believe that it drives the best-in-class incentive plan, but also more importantly lines up with our strategic direction that we're taking.

Adam Tindle
Analyst, Raymond James & Associates, Inc.
Q

Okay. And just to clarify on near term, you talked about not planning to meet guidance for the March quarter. Does that mean not meeting the low end of guidance, the midpoint of guidance? Just any frame of reference would be helpful just as a housekeeping item. Thank you.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.
A

Yeah. So I'd say, Adam, at this point we're still evaluating the situation, and I hope you guys understand this. Everybody I've talked to said that they'll do because things are changing every day. We have a couple more weeks to close the quarter, and we're trying to understand how we keep our operations running in parts of Europe and US as things unfold. So it's hard for me to give you a very clear number because it really depends on how much of our factories are running. Right now the good news is we have China back in track, lots of our operations across the world are running, expect parts of Europe, but this is an ever changing situation every day.

So while I'd love to give you a very good well-defined number, I just don't think that it's prudent to do this at this time because every week we have different shutdowns and different scenarios being executed by federal governments and state governments across the globe. And that makes it difficult for us to figure out what revenue we can ship. I will say clearly, Adam, that but we are managing this in a very comprehensive way. We gave a very full update on what we're doing, and very comfortable as we come out of this, that we will be well-positioned to show that we manage this the best for all our stakeholders.

Adam Tindle
Analyst, Raymond James & Associates, Inc.

Q

Understood. Thank you.

Operator: Your next question comes from the line of Mark Delaney from Goldman Sachs. Your line is open.

Mark Delaney
Analyst, Goldman Sachs & Co. LLC

Q

Yes. Thanks for taking the questions, and I appreciate all the work that went into the presentation. I wanted to follow up on the operational realignment over time and potential factory optimization. Is that something that Flex intends to do in a relatively near term in terms of moving where some of the products are manufactured and leading to some footprint optimization potential, or is that more of a long-term possibility that as programs for rebid that that would be the time to potentially move those?

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

Mark, thank you for that question. We've already started this work. We did a very comprehensive look at our footprint and what room we have for optimization, but also what is the right model for us moving forward. So this work has already started. We have a very clear game plan of what we're going to do in terms of the next year, the next two years. So we have a very well-defined framework. So I view this as a very short-term, mid-term work that we are undertaking. And then what it leads into is that in the future we'll be more well-positioned to really drive our manufacturing footprint to the strategy that we're laying out. So no, we're very mature in this work, and we're well on our way to executing a lot of what we've laid out today.

Mark Delaney
Analyst, Goldman Sachs & Co. LLC

Q

That's helpful. And then, I realize mix is always an important dynamic for margins. But in terms of getting to the 7.5% or 7.5% plus gross margin, is there any certain minimum revenue levels you think the company needs to be in order to achieve that?

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

Well, we're trying to plan with a range, because what really is important to hit that margin ranges is to be flexible for us to make sure that we can move our overhead structure and our manufacturing structure that flexes with the revenue. We just hit 7.1%. So I'm assuming that it's not a huge stretch for us to get to the 7.5%. Now, that doesn't mean we're sandbagging or anything. We have work to do to get what we're laying out here. But we did that with taking out $1.2 billion of underperforming revenues. So my view Mark is that good businesses know how to migrate their business models based on their mix.

Mark Delaney
Analyst, Goldman Sachs & Co. LLC

Q

I got it. And then just one last one for me, is the company is shifting where it does its manufacturing and the operational realignment? Are there any ramifications for the tax rate? I think that the prior guidance was midteens. But I'm wondering if we needed a completely different number as you change where you're doing business. Thank you.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

Chris?

Christopher E. Collier
Chief Financial Officer, Flex Ltd.

A

Hey Mark, thanks for the question. No, I would say that as you think about our geographic dispersion already it's reflective in a rate that's been in the range of 10% to 15%, and we've been at the higher end of that range. We do not see anything as we move these capacity shifts in realignment of our business to these new delivery models that will result in anything meaningfully different than how we've been guiding everybody.

Mark Delaney
Analyst, Goldman Sachs & Co. LLC

Q

Thank you.

Operator: Your next question comes from the line of Paul Coster from JPMorgan. Your line is open.

Paul J. Chung
Analyst, JPMorgan Securities LLC

Q

Hi guys. It's Paul Chung on for Coster. Thanks for taking our questions. So just on the corona impact, so starting to get a better sense for supply and capacity utilization with your China facilities kind of ramping back up, and thanks for that update. But how have you seen demand impact from your customers? Are you seeing some hesitancy, maybe some delays and postponements, and are there parts of the business where you've seen kind of outright cancellations that may not come back?

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

So Paul, thank you for that question. I think we gave you a way in terms of how we're thinking about the scenario planning, and how we're looking forward at calendar year Q2, Q3 and Q4. So if I think about our diversity of our segments, each one reacts a little differently is what I would say. If you think about our medical customers and some of our automotive customers, most of them need the revenue, want the revenue, wanted it yesterday, and we have to really push to ramp those back as quickly as possible. And that's what's happening, and that's very similar in our industrial customers too. I would say, our CEC businesses just already had a slower year as you all know coming into the quarter and the year that was driven by kind of in general 5G ramp and tech slowdown. And I think they will continue to see that which is what we're kind of assuming in our model for the next few quarters.

And for our lifestyle business, I mean it all depends on consumer spending and how consumer spending reacts in the next few quarters, and that will drive how our lifestyle business looks, I would say, in the next few quarters. But if you bring it all together, what we're doing is saying, we're going to be cautious in our planning because we have such a big view of the diversity of what happens with the end market demand, and we're saying that some are going to go up over the next couple of quarters, some are going to be flat to down, and overall we're kind of planning for Q2, Q3 to continue to be at the levels that we're seeing right now, with maybe a recovery at the tail end of the year. So that's kind of how we're assuming. But I know all of you know that your crystal ball is as good as mine, and we're all trying to understand how this plays out.

Paul J. Chung
Analyst, JPMorgan Securities LLC

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Got you. And then on competition, so where are you seeing kind of that lower-margin business that you're [indiscernible] (01:33:55) kind of going to, and then kind of giving your pricing discipline, are you seeing more of the rational pricing environment? And then kind of lastly, are you seeing customers you've initially kind of called from the portfolio kind of come back and pay up for your services if you could give any kind of examples if that is indeed even happening?

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

So I'm going to maybe give this to Doug and Paul to jump in here overall I'd say. In terms of where competition is going, it really I'd say is irrelevant to us. I'm sure there's enough people in the world who want that kind of business. But maybe talk about pricing discipline and customers a little bit. So Doug maybe you start, then Paul.

Douglas Britt
President-Integrated Solutions, Flex Ltd.

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Yeah. Sure. In each one of the markets that we address it's a little different, the computation is different. If I take the consumer devices business, what we're concentrated on is making sure we generate very solid ROIC and free cash flow generation, and making sure that we're engaged with customers that have multiple product lines. So we can keep heavy utilization in our factories where we've been challenged, and that business has always been where we have customers that have narrow product families, where we have significant transition change and that revenue goes down impacts our utilization.

So from a pricing standpoint what we're focused in on very solid terms and conditions around our cash flow. Our CEC business where we're adding value around design. We're able to extract higher value, higher margins, and then we have some very large customers that demand market pricing, and we position ourselves there and we differentiate with a bundling of services to move the margin up, so it might be repair, could be asset recovery, we're doing manufacturing, we're doing bill-to-order and you stack all those services together and we're able to compete where some of our competitors don't have that breadth of service offering.

Paul J. Humphries
President-High Reliability Solutions, Flex Ltd.

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And from Reliability standpoint, I think the way that we've approached it, and we've talked about this previously, is we're not focused on the commodity type products in the industry. We're looking where we can bring value either through technology, operational capability and our differentiation in other ways. So we're bringing value, but isn't typical of what you see in the commoditized business. So there's always price pressure, but with [indiscernible] (01:36:42) strategy we think [indiscernible] (01:36:41) and drive margins higher.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

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So then Paul, I'll just bring it all together and say is that, I think we are revisiting where our growth comes from, and we are redefining ourselves as a different kind of business. And with that comes selling value to customers and having pricing discipline. But in terms of customers itself, I have very good relationship with many of our CEO customers, and they all understand what we are trying to do in terms of providing value to them. Most importantly, most of our customers want us to do more. They want us to do more in terms of design, more in terms of manufacturing. They want us to take over what are tricky issues for them that they think we're well positioned to do. And I have very good connections with our top CEO customers. And I would say that they see this as an effective strategy. That's what they want us to be, to be a good long-term partner. And I would that is how you should view our relationships playing out, and why this strategy makes sense for us and our customers.

Paul J. Chung
Analyst, JPMorgan Securities LLC

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Okay. Great. And then last question just on capital allocation. So your business model particularly on the Reliability side kind of provides nice visibility into cash flows, kind of longer term, which is supported dividend in this kind of low rate environment. What's your thinking behind that path, because as I look at the stock price over the past five years, it's not much different? So granted we have some shocks in tariffs and corona, but just want to hear your thinking there. Thanks.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

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Paul, I'd view it differently. I'd say if you think about the last five years, I mean, this business has gone through a lot of transition and change. I think, if you think about the last year and what we have done in the last year, even working through trade and corona issues really should be the benchmark to use in terms of where the future of this business goes. And I think we have been great stewards of capital if you look at the last 12 months. So I think that's how we should be judged, and that's how we should think about this business moving forward.

In terms of capital allocation, Chris made it very clear that we clearly understand that we want to buy back more of our stock, and we will do that in 2021 pending all these issues that are happening in the marketplace and that's our goal. But we'll also do it based on kind of timing of our stock price and based on other investments we want to make, and we will be good, very cautious investors, and I think that's what our shareholders want, and I think we'll do that well. In the last year I had shown that we've got a good framework, we've executed that well and we'll be focused on it. If our stock price is at the light level, we'll continue to buyback more, and we think that we have room to do more of that in the next year.

Paul J. Chung
Analyst, JPMorgan Securities LLC

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Thank you so much.

Operator: Your next question comes from the line of Steven Fox. This is our last question and it's from Fox Advisors (sic) [Cross Research] (01:40:06). Your line is open.

Steven Fox
Analyst, Cross Research LLC

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Thank you. Good morning. Thanks for taking my question. Two questions if I could, first of all it seems you guys seem to suggest that given the success of the Buffalo Grove facility that is leading to other new business. And I was curious that that sort of fully vertically-integrated customer-specific factory seems unique within the Flex footprint. Does that mean that you would pursue more factory or footprint like that or how would these add-on businesses look down the road? And then secondly, can you just talk about how you incentivize technology sharing across the two business units since its seems like designs are dependent on having the full footprint or the full playbook of design available to both sides of the business? Thanks.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

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So Steven, I'll start and hand it over to Paul. I'd say, absolutely we are taking on more work that looks like the Buffalo Grove work where we are providing more than one solution to a customer, and where our products are more end-to-end. And we're doing that not just in our health solutions space but even in our Agility space and our automotive space. So more of not just electronics but wrapped around all the mechanicals, all the connectivity, a full holistic platform is what we're looking to deliver to our customers. And we have already added more examples like that to the wins. Just in the CGM space we are one of the largest growing manufacturers, and our plan is to continue to focus on that. Doug gave a great example of the floor care example where we're fully vertically integrated end-to-end in terms of that type of product that we're providing our customer.

It provides more customer affinity and a longer life cycle, which is what we like about that. And then on the technology side, technology is always in matrix. There are areas of technology that clearly is driven and owned by the segments, and that's what we're pushing for that they understand what they own and they take to market. And then there are areas like we discussed the power example, the autonomous example that we will leverage across the business. And we have Paul, runs our central technology organization today. We continue to have a role like that who will look across the platform and make sure technology sharing happens. And Steven, this is quite common in most of the spaces that I have worked in, that you have a dedicated technology organization and you have something that leverages it across the business, and that's how we'll continue to do it. So any additions, Paul?

Paul J. Humphries
President-High Reliability Solutions, Flex Ltd.

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Yeah. I mean, in terms of the CGM business, we've already secured another site that's already qualified for medical grade manufacturing, and agreed that with the customer, and are actually in the process of working to start up that facility. So we already have identified an alternative facility to Buffalo Grove. I don't want to disclose which one it is at this point. But again, we're very, very confident that we have the capacity available to expand into the new products. On the technology side, the segments obviously have control over the direction that the engineering teams work on in regards to the products that they work and the investments that they have, the customer applications that they go after.

But we still have a central group that focuses on things like tools, systems, processes, best practices, and looks across the entire organization to ensure that we're leveraging the cross-functional capability that exists within our design organizations. And we've mentioned about the power business, the auto compute business and the battery business are some examples where we're doing that. That organization is still in place. We're still making sure that we are leveraging the whole as well as obviously optimizing the capability for each segment. So I don't see a significant change other than obviously there's more focus directly on the segments that there might have been previously.

Steven Fox
Analyst, Cross Research LLC

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Great. That's very helpful. Good luck going forward. Thank you.

Paul J. Humphries
President-High Reliability Solutions, Flex Ltd.

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Thank you.

Revathi Advaithi

Chief Executive Officer & Director, Flex Ltd.

Hey. Thanks, Steven. And that was the last question. I'd like to thank all of you for joining us today and taking the time to talk through our new strategic direction. As you can tell, we are holistically changing our strategy, our organizational and our operational model, our values, our culture and our incentives. And we believe that this is a great first step in our transformation journey. Thank you all for joining us.

Operator: Ladies and gentlemen, this concludes today's conference call. Thank you for participating. You may now disconnect.