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EDITED TRANSCRIPT

ST - Q1 2016 Sensata Technologies Holding NV Earnings Call

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PRESENTATION

Operator

Good morning, and welcome to the Sensata Technologies Holding NV first quarter 2016 earnings webcast. At this time, I would like to inform you that this webcast is being recorded. For opening remarks and introductions, I would like to turn the call over to Jacob Sayer, Vice President of Treasury and Investor Relations. Mr. Sayer, you may begin.

Jacob Sayer - *Sensata Technologies Holding NV - VP of Treasury and IR*

Thank you, Keith, and good morning, everyone. Earlier today, Sensata issued a press release describing its financial performance for the first quarter 2016. You may obtain a copy of the press release and the slide deck that we will be referring to in today's webcast from the Investor Relations section of our website at Sensata.com. A replay of today's webcast will also be available in the Investor Relations section of our website.

Today's discussion will contain forward-looking statements based on the business environment as we currently see it and as such, it does include certain risks and uncertainties. Please refer to our press release and our 10-Q and 10-K filings for more information on the specific risk factors that could cause our actual results to differ materially from the projections described in today's discussion.

In addition to US GAAP reporting, we report certain financial measures that do not conform to Generally Accepted Accounting Principles. We believe these non-GAAP measures enhance the understanding of our performance. Reconciliations between GAAP and non-GAAP measures are included in the tables found at today's press release and slide deck, as well as in the Investor Relations section of our website under financial reports. Comments made during today's call will primarily refer to our non-GAAP financial results.

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On the call with me today, are Martha Sullivan, Sensata's President and Chief Executive Officer, and Paul Vasington, Sensata's Chief Financial Officer. We will hold questions until after our prepared remarks, but if you'd like to get in the queue, please do so by pressing the star key followed by the number one.

I'll now turn the call over to Martha, to review highlights from the quarter and trends in the end markets that we serve. Martha?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

Thank you, Jacob, and thank you all for joining our first quarter 2016 conference call. Sensata's strategic goal is to win in sensing and by doing so, to continue to create long-term value for our shareholders. During today's call, we'll highlight a number of ways this takes place.

So let's start with the first quarter results. We delivered 6% revenue growth driven primarily by acquired revenue. We also grew adjusted net income by 8% before the impact of foreign currency exchange rate. This was due primarily to integration synergies and operational efficiencies. This is a good start to the year, slightly above the midpoint of first quarter guidance and putting us on track for the full-year.

Sensata creates value for our shareholders by expanding margins. In addition to margin growth in the core business, we are on track with integration activities at each acquisition to deliver further margin expansion. While acquisitions dilute our margins during the integration phase, we are on track to achieve our long-term adjusted net income target margin of 20% to 23%.

I would also like to highlight a few key ways Sensata grows revenue. Our organic growth benefits from the ongoing increase in regulations, among other things, that push for safer and more fuel efficient vehicles as well as a cleaner environment. We're on a regulatory journey that underpins sensor content growth for years to come.

In addition, acquisitions provide further revenue growth and propel Sensata into new sensing markets and technologies. The acquisition of the sensing businesses in CST closed in December, and the integration of those businesses is proceeding according to plan. CST extends our end market growth opportunities beyond automotive, adding 10% of nonautomotive revenue. Encouragingly, we have already logged some early design wins, demonstrating the need for sensors among industrial customers.

We're very pleased to announce during the quarter, an expansion of our technologies critical to the adoption of advanced driver assistance programs. Quanergy, the leading developer of solid-state LiDAR technology, and Sensata, are now exclusive partners in the development of component level LiDAR sensors for transportation markets. This is an exciting and potentially very large future sensing application.

And finally during the quarter, we reduced our net leverage ratio to 4.5 times through strong free cash flow generation and we paid down a portion of our outstanding revolver.

Sensata's core margins of 18.4% in the first quarter, or 19.6% on a constant currency basis, expanded by 80 basis points from the first quarter of 2015. On a reported basis however, Sensata's margins are naturally diluted by the lower standalone margins of acquired businesses plus integration costs.

Despite this, adjusted net income per share has grown at a double-digit pace to the four years shown on slide 4. Part of the investment thesis for each transaction includes integrating the acquired business, improving the margin and then bringing it into the core.

Core margins, excluding the impact of acquisitions and foreign currency movements, remain high. The Honeywell Onboard and SensorNite acquisitions are fully integrated and included in the core margin for all periods shown. Wabash, in an acquisition completed at the beginning of 2014, is included in the core line for 2015 and 2016.

We control our destiny by implementing our integration playbook, we improve acquisition's operating efficiency, enable revenue growth, globalize each business and raise their margins over time. As we fully integrate DeltaTech, Schrader and CST, and additionally, improve the performance of

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the core business, we expect the reported margins of the business to rise in the coming years and to reach our target adjusted net income margin range of 20% to 23%.

Regulations are not a one and done affair. As you turn to slide 5, you can clearly see that we are on a regulatory journey around the world, stretching out as far as 2025. Our Euro VI B emissions regulations have rose substantial content growth for Sensata last year in Europe. There are many more regulations to come. This helps drive content growth for Sensata as the technologies necessary to comply with regulations are adopted.

It is important to note, that regulations are not the only driver to content growth, but just one of many. There are plenty of examples of OEMs adopting sensors and their systems to simply drive productivity or convenience. Advanced operator control systems being adopted by heavy vehicle OEMs today, using position sensing technology from Sensata, is a good example of this.

A couple of advancements in the quarter that you may not be aware of include crankcase pressure sensors. This is a new category of design wins in the first quarter.

Onboard diagnostic requirements in North America, will soon require a positive confirmation that crankcase gases are not leaking into the atmosphere. A combination of Sensata and Schrader improves our competitiveness in low-pressure sensing, helping to enable a number of design wins in this area.

And real driving emissions requirements tightened the emissions levels of vehicles on the road. To address this in the future, OEMs will need to introduce particulate filters on a wider range of vehicles. These filters require pressure and high temperature sensors or where we have also had new design wins in the first quarter.

In addition to organic growth led by new design wins, acquisitions are an important part of our value creation strategy. Through the process of integrating acquired businesses using Sensata's proven best operating practices, we grow the earnings power and the margins of the business. CST adds 10% of non-auto revenue to Sensata, extending our secular growth opportunities into the industrial and aerospace end markets.

We are also excited to report some early design wins with CST during the first quarter. A leading climate control specialist has designed our pressure sensors into their next generation of industrial chillers. This win was enabled by the expanded industrial sensing capabilities brought by CST, combined with the world-class quality and delivery reputation of Sensata. Additionally, during the quarter, we were awarded a design win by a major aircraft OEM to add highly sensitive LVDT position sensors to their autopilot system in next-generation aircraft.

Another event we're really excited about is our strategic agreement with Quanergy. In March, we announced strategic partnership and investment agreements with Quanergy Systems, the leading developer of solid-state LiDAR technology to advance the ongoing development and commercialization of LiDAR sensors. LiDAR sensing is expected to be a mission critical component of future advance driver assistance systems, including semi and fully autonomous driving, especially in the 2020 to 2025 timeframe.

Quanergy and Sensata are now exclusive partners for component level solid-state LiDAR sensors for the transportation market. This strategic partnership is a pragmatic way to extend our sensing capabilities into advanced driver of systems applications, one of the fastest growing areas of the transportation sensing. Quanergy will continue to lead LiDAR technology development activities, while Sensata will focus on automotive quality product development and manufacturing and will own the customer relationship. Together, our goal is to deliver solid-state LiDAR sensors that have substantially lower costs, higher reliability, improved capability and lower power consumption when compared to traditional mechanical LiDAR sensors.

According to industry experts, the LiDAR market is expected to develop into a $1 billion market opportunity by 2020, and we're confident that our long track record of bringing new sensing parameters to customers and implementing successful global rollouts, will enable us to make this important opportunity a success. Customer engagement is underway and we have seen substantial consumer interest in full.

I would now like to turn the call over to Paul, to review our first quarter results in more detail and to provide financial guidance for the second quarter and full-year. Paul?

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Paul Vasington - *Sensata Technologies Holding NV - CFO*

Thank you, Martha. Key highlights for the first quarter as shown on slide 8, include net revenue of $796.5 million, an increase of 6% from the first quarter of 2015. Of this, acquisitions less exited business contributed 8.9%. Organic revenue was down 0.9% and changes in foreign currency exchange rates, primarily the euro, represented a net revenue headwind of 1.9%, all consistent with our expectations.

Adjusted net income was $113 million, or $0.66 per diluted share and slightly better than expectations. When compared to the prior year, adjusted net income grew 2% in the first quarter, or 8% on a constant currency basis, primary due to productivity improvements and integration synergies.

Adjusted net income margins declined 60 basis points to 14.2% in the first quarter. However, excluding CST and the impact of foreign currency, adjusted net income margins expanded 130 basis points from the prior year to 16.1%. In the core business, which excludes DeltaTech, Schrader and CST, adjusted net income margins were 18.4% in the first quarter, or 19.6% on a constant currency basis, up about 80 basis points from the prior year.

Favorable impact of foreign currency exchange rates was $0.04 in the first quarter. The first quarter included benefits from outstanding hedge contracts that will decline during the course of 2016. Consequently, we continue to believe there will be a detrimental impact from changes in foreign currency exchange rates of $0.17 to $0.21 for the full-year.

Integration costs were $3.5 million in the quarter. Restructuring and special charges of $3.6 million, added back to our non-GAAP numbers in the first quarter, were primarily related to improving operating efficiency and aligning our cost structure and business models to end market performance. These charges appear in the cost of revenue, selling, general administrative and restructuring and special charges lines in the GAAP income statement.

Cash taxes in the first quarter, were approximately $10.4 million, 6.4% of adjusted earnings before interest and tax. For the full-year 2016, cash taxes are expected to be approximately 6% in adjusted earnings before interest and tax. This is in line with our cash tax guide of 5.5% to 6.5%, which was updated when we acquired CST.

Now, I'd like to comment on the performance of our two business segments. Side 9 details the performance sensing business unit, where we achieved net revenue of $597 million for the first quarter, up 1% from the year ago quarter as a result of acquired revenue and new program launches, especially in Europe and China, offset somewhat by the impact of annual price downs and changes in foreign currency exchange rates. Also as expected, we saw further declines in the heavy vehicle and off-road market, especially on-road heavy trucks in the US.

Performance sensing profit from operations was $146 million, up 1% from the year ago quarter, primarily from higher volume less the impact of foreign currency exchange rates. Performance sensing profit from operations index of 24.4% was up a little from the first quarter of 2015, despite foreign exchange headwinds, due primarily to net productivity gains, including cost synergies, from acquisitions.

Sensing solutions net revenue was $199 million for the first quarter, up 25% from the year ago quarter, due primarily to the impact of acquired revenue from CST and down 7% organically due to weak demand in certain end markets affecting weak global economic conditions. China remained weak in the first quarter year-over-year, but showed sequential growth. Consequently, we still believe we will see improving sequential year on year results from our solutions business in China during the balance of the year.

Sensing solutions profit from operations was $63.2 million, an increase of 29% from the same quarter last year, primarily due to higher volumes in productivity gains that drove an 80 basis point increase in margin from first quarter of 2015. Our team performed very well in delivering profit margin improvements in a tough market environment. Corporate and other costs not included in segment operating income, were $44 million in the first quarter.

Free cash flow for the first quarter $102 million, was attributed to higher net earnings adjusted for non-cash items and good working capital management during the course of the quarter. This cash was deployed upon our investment in Quanergy and to repay debt, which helped lower our net leverage ratio to 4.5 times. Details of our financial guidance for the second quarter of 2016 as shown on slide 11, are as follows.

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Net revenue of $820 million at the midpoint, which is an increase of approximately 6% from the second quarter of 2015, reflecting the balance of performance sensing flat to up 1% organically, reflecting strength in our core automotive business offset by weakness in the heavy vehicle off-road market reflecting worsening on-road production. A low to mid single-digit decline in sensing solutions, its acquired revenue growth approximately CST, a 1% headwind from exited businesses and a 2% to 3% headwind from changes in foreign currency exchange rate.

Our current fill rate stands at approximately 84% of the midpoint of this guidance. Adjusted net income of $122 million at the midpoint and adjusted net income for diluted share of $0.71 at the midpoint, which includes $0.05 to $0.06 of detrimental foreign exchange impact and a fully diluted share count of 171.6 million shares.

Our financial guidance for the full-year 2016 remains unchanged from when we initiated guidance during our prior earnings call at the beginning of February. Sensata maintained a very strong balance sheet. Our strong and stable free cash flows have enabled us to reduce leverage in the past. Prior to the acquisition of Schrader, we operated within our target net leverage range for an extended period of time.

While financing the acquisitions of Schrader and CST temporary inflate our net leverage ratio, we're on track to lower this to 3.7 to 3.9 times by the end of the year. Our near-term goal is to lower the net leverage ratio and barring any new acquisitions, we expect to be about 3 times net levered by the end of 2017.

Now, let me sum up by turning to slide 13. Sensata is a leading industrial technology company, but more importantly, we're the largest independent supplier of sensors in our sector. Sensing is an attractive growing market and we've been in this space for over 25 years. We are better positioned than anyone else to be successful in this environment.

From 2013 to the midpoint of our guidance for 2016, net revenue and adjusted earnings per share have experienced compound annual growth of approximately 13% and 10%, respectively. Increasing sensor content drives sector growth and enables us to grow faster than our end markets. Further, M&A is a strategic pillar of our growth strategy, enabled by strong cash generation and a disciplined acquisition and integration process to ensure strong financial returns.

Sensata is a high margin high cash generation business. Our margins are born out of long cycle revenue, highly differentiated products and extremely cost-effective manufacturing operations. Strong margins coupled with a low cash tax rate, drive strong free cash flows, which allow Management to generate industry-leading returns for investors.

We're committed to creating significant value for shareholders through the combination of double-digit revenue and earnings growth, standing operating margins and superior capital deployment.

We're now happy to take questions at this time. Operator, please introduce the first question.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Wamsi Mohan, Bank of America Merrill Lynch.

Wamsi Mohan - *BofA Merrill Lynch - Analyst*

Yes, thank you. Good morning. Martha, when we take a step back and just look at some of the largest headwinds in 2016, there were China industrial, it was HVOR and FX. And seems from your comments that most of those are starting to stabilize. Can you share some color maybe in terms of the other patterns that you are seeing in industrial in China in particular? Any comments on HVOR will be helpful and I have a follow-up.

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Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

Sure, Wamsi. I would say on HVOR, it is really developing as expected. As you know, it is the on-road piece that is the most beleaguered. We think our call is right. We think we have definitely seen things like inventory stabilize over time and we're performing really well. So if you look at how we're performing versus how down that market is, it really gives you a sense for the strength of Sensata's content growth.

On China for Sensata, it's a tale of two markets. And the auto side, we've actually seen a rebound of the production rates as we saw the inventory corrections in the third and fourth quarter last year. We're watching it closely. We think that there may be some vehicle inventory building in the first quarter in China. That is played into our guide and as we look forward. But we've seen pretty substantial recovery in that market.

On the industrial side, I would say much less so. Again, playing out as expected. So you are seeing sequential improvements in the industrial China part of our overall business. Again, that is what we expected. We're watching that PMI manufacturing index in China pretty closely and that has stabilized. Again, similarly for currency, just given our hedge positions, we think we have that well contained.

Wamsi Mohan - *BofA Merrill Lynch - Analyst*

Great. Thanks, Martha. And as a follow-up, could you just give us some perspective on LiDAR adoption? How you think about it with respect to where solid-state LiDAR is priced today? Do you think the pricing needs to come down materially for adoption rates to pick up? And, when you think about the incremental content that LiDAR can drive, on a per vehicle basis, could you give us some sense of that? Is that in the $5 to $10 range or is the opportunity bigger? Thank you.

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

Sure, Wamsi. If you look at what's out there today, it is really mechanical LiDAR. That is just extremely high-priced, so think thousands and tens of thousands of dollars on mechanical LiDAR systems. Solid-state LiDAR is really a phenomenon that needs to be commercialized and get to the quality and reliability performance that we need in auto. And it will be a game changer.

So now, we are pricing in the hundreds of dollars. That figure alone ought to give you a sense for the content per vehicle. And there are scenarios that have more than one solid-state LiDAR sensor on board say a fully autonomous vehicle or at least one. So we decided a figure of $1 billion market when get into the 2020 through 2025 timeframe. Those are some of the puts and takes that are driving that figure.

Wamsi Mohan - *BofA Merrill Lynch - Analyst*

Thanks, Martha.

Operator

Steven Fox, Cross Research.

Steven Fox - *Cross Research - Analyst*

Thanks, good morning. I was wondering. You touched on China a little bit, but broadly speaking on industrial, when you look at supply chain versus on demand and your expectations for the rest of the year. It sounds like it is tracking, but can you give a little bit more detail on how you might see that play out over the rest of the year, especially as you get into the summer months? Thanks.

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Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

We're watching inventory carefully there and we think much of that has corrected. I would say one notable exception, and it's becoming a much smaller part of our business, but we supply into compressors for HVAC and China. And there's still a pretty high level of inventory of HVAC compressors. So, that is one area where we continue to see higher inventory and again, have that played out coming down gradually month by month.

The balance of our business in China and now I think $140 million in revenue in total in industrial in China, is really moving along the bottom as expected at this point. We're not expecting a lot of recovery as we go through the year. We do get into more favorable comps year-over-year as we move into the second half of 2016.

Steven Fox - *Cross Research - Analyst*

Great. That's helpful. And just to double check on the acquisitions, which again, also seem to be proceeding as you expected. Is there any opportunity to pull in some of the cost savings as you go through the year or do you think when we look at this from the outside, we're not appreciating some of the complexities that you are dealing with? How would you describe potential upside with the acquisitions between now and year-end?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

Important to understand is often that synergy comes through moving manufacturing. So we are doing these in end markets where quality and validation are a big part of the overall process. For example, we announced the closure of our Tennessee plant related to the Schrader acquisition in the fourth quarter. So these are safety related componentry that we'll be moving from Tennessee into our Mexico site. We look for every opportunity that we can to get that done more quickly, but we do have to work closely with our customers as well. So I think that there's opportunity. At the same time, it's really important that we do no harm as we integrate these acquisitions into Sensata.

Steven Fox - *Cross Research - Analyst*

Great. That is very helpful. Thanks so much.

Operator

Craig Hettenbach, Morgan Stanley.

Anil Agarwal - *Morgan Stanley - Analyst*

Hello, this is an Anil, calling in for Craig. I had a question on the Schrader business. You talked about the China regulation as a potential growth driver for that business in the future. What are your expectations for growth longer-term for that business? And as a housekeeping, could you just provide us what was the EPS contribution for Schrader this quarter and what is the expectation for the full-year?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

It is very difficult as we move forward and we get more intertwined with these acquired businesses to break out EPS on something that is now been inside of Sensata for as long as Schrader has. At the same time, I will tell you we actually delayed some of that integration because we had a ramp in Europe. So we our spending on Schrader, I'd say fairly significantly this year.

To get back to your question about China regulations, we expect that to hit in early 2019. We expect the revenue associated with the regulation to hit in that timeframe. China now being one of the largest automotive markets, think 17 million vehicles, and a mandate across that fleet of four

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sensors per vehicle is a pretty large opportunity. And if we were to simply hold our share, we would expect to see at least 30% of that overall volume for Sensata.

We have seen some interesting developments that may actually create some revenue for us in tire pressure sensing in China ahead of the mandate. There are insurance benefits now recognized to monitoring tire pressure sensing and we're seeing some adoption from OEMs ahead of their regulation. So as we look between now and 2019, we do expect TPMS is going to be a great growth driver for Sensata.

Anil Agarwal - *Morgan Stanley - Analyst*

Got it. That's helpful. A high level question, when you look at the 2016 guidance, you're calling for organic growth between 0% and 3%. Is high single-digit organic growth still available for the business when you look at a normalized economic environment? And when you look at next year, I know you're not providing 2017 guidance, but what do you think at a high level are the key drivers that will lead to a pickup in growth?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

Yes. So, you're right, we're not providing guidance for 2017, but let's just look at them things that we have talked about and they can give you a sense for it. We do think that strong organic growth is a really important investment basis for Sensata and it continues to hold very well just given the design wins that we're seeing and actually some of the early progress on the acquisitions related to top line growth as well.

One of the things that I think has changed for Sensata, if we reflect on second half of 2015, we have recognized that there is a portion of our business in sensing solutions, call it more of the legacy controlled business, represents about 12% of our revenue that is not going to see China as the growth driver that it has been. That portion of the business will grow much more slowly, if at all. We've talked about 0% to 1% growth in that overall business. That is the expectation we have for that portion of sensing solutions over the long-term.

I will point out though that we see we continue to see great earnings potential even in that business. So the combination of organic growth that is available and the balance of Sensata and continued good earnings growth in that portion of our sensing solution, I think is a great value opportunity for investors.

Anil Agarwal - *Morgan Stanley - Analyst*

Got it. That is helpful. Thank you.

Operator

Christopher Glynn, Oppenheimer.

Christopher Glynn - *Oppenheimer & Co. - Analyst*

Thanks, good morning. It seems like a lot of things are playing out just as you expected, perhaps even more so than normally. So I was just wondering with the shifted dynamic in the auto cycle probably looking pretty mature, I'm wondering if that impacts the normal phase in of the annual price downs or if that is just a carbon copy of recent years, how that layers into your model?

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Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

Chris, this is developing very naturally. We're used to seeing the pricings hit early in the year. Our first quarter, generally, is where we will see that happen. You see that play out on the performance sensing side of the business where we have the multi-year contracts. I would say no, we're not seeing anything cycle driven that is changing the overall pricing dynamic.

Christopher Glynn - *Oppenheimer & Co. - Analyst*

Okay. And you're on track with all of your sourcing initiatives to offset that and everything?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

We are. Very much so.

Christopher Glynn - *Oppenheimer & Co. - Analyst*

Great. And just as you've had a little experience with CST under the hood for a while now, I'm just wondering how you feel about the overall critical mass of Sensata in the industrial side? How that feeds off the auto and just the idea of the importance of critical mass facing the industrial markets as opposed to the traditional automotive?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

Right. It's a great question and it is something that we think about and we plan around a lot when we make these acquisitions. It is a much more fragmented market, as you know, and even inside of the vertical aerospace machinery, there are niches as well. So what we think is really important is to find defensible barriers and applications and in portions of that overall market. At the same time, it gives us just a great line of sight on where we can intercept other niches, both organically and inorganically. So this industrial space is a really attractive one for Sensata.

Christopher Glynn - *Oppenheimer & Co. - Analyst*

Thanks.

Operator

Mark Delaney, Goldman Sachs.

Mark Delaney - *Goldman Sachs - Analyst*

Good morning. Thanks very much for taking the questions. First question is a follow-up on Quanergy. Can you talk about the financial implications of revenue as you start to realize it with that relationship given that are going to be selling a product design by somebody else? If you could help us think through the gross margin and operating margin profile of that business? And then related to that, as you go forward, do you think there's an opportunity to jointly develop products using Quanergy's solid-state LiDAR as with some of Sensata's initial on hand sensors that you already have?

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Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

I think the answer to the first question, we have to be a little bit careful here. What the agreement calls for is a fairly even split of overall earnings as we get to revenue over time. So while the core technology around LiDAR sensing is very much in the hands of Quanergy and some terrific experts that sit inside of that entity, there are packaging challenges as well, and IO challenges in terms of different customers where Sensata is going to bring some expertise even to the core LiDAR sensing that would go into autonomous vehicles.

When you think about margins, we think this fits really well with Sensata's overall margin profile and that is important. It was an important consideration for us as we looked at the overall agreement. So pretty attractive. And yes, I do think as we work together, there is opportunity to do more and to integrate overtime. I will tell you, our approach to the market though is one of independent component level sensor suppliers and we've got some great system levels, some partners, inside of ADAS. We do not see ourselves operating at the system level.

Mark Delaney - *Goldman Sachs - Analyst*

That is helpful. And the follow-up question is related to the earthquake in Japan. There's been some talk from a few of the auto companies about changing their production schedules for a short period of time. Are you seeing any volatility related to that issue?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

We have not yet seen volatility in the order demand, but we have reached out just to understand that dynamic a little bit better and to understand if it might have an impact in the second quarter here. As we understand it, the assembly plants where that is being impacted are operating below capacity and there's good opportunity to recover that downtime inside of the quarter given that they are doing it fairly early.

Mark Delaney - *Goldman Sachs - Analyst*

Thank you very much.

Operator

Amit Daryanani, RBC Capital Markets.

Amit Daryanani - *RBC Capital Markets - Analyst*

Thanks a lot. Good morning. Two questions from me as well. First, could you start with the AR increase you guys saw in the quarter? What drove that and was there anything on the linearity in the quarter that impacted it?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

Amit, we're having trouble hearing you. Can we hear that one again?

Amit Daryanani - *RBC Capital Markets - Analyst*

Hopefully, this is better. I was wondering if you could start off talking about the accounts receivable increase that you guys saw in the quarter? Was there something that drove that one-off or was there something to do with the linearity you guys saw in the quarter?

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Paul Vasington - *Sensata Technologies Holding NV - CFO*

It's linearity. We ship per our customer's request and the revenue was (technical issues). No issues around collectibility.

Amit Daryanani - *RBC Capital Markets - Analyst*

Perfect. Back to strategic investment in Quantergy. Could you just talk about what drove that decision versus perhaps trying to build out your own solution there as it relates to the autonomous markets? Broadly, is this strategic investment enough to give you a portfolio there or do think we need to do fully to broaden out the portfolio be that organically or through acquisitions as you go forward?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

To be clear, if you look at the level of technology involved in LiDAR, particularly solid-state LiDAR, that has been years and years in the making. If you look at the background of some of the folks on the LiDAR team, particularly (inaudible) himself who is the founder of that business, that would take years to do on an organic basis.

Given the overall value of that sensor, we think it is a great content position for Sensata as we get to semi and full autonomous vehicles. At the same time, I would just remind you, we actually do have content today that plays into ADAS adoption. And we're seeing lift in that area as we look ahead.

So, one of the foundational systems that needs to be in place are things like advanced braking systems and emergency braking. And that requires sensors and stability control systems where we are very well-positioned today. So there are some things that we are drawing on already inside of Sensata's core portfolio. The LiDAR play really allows us to play in that space as it goes autonomous in a very meaningful way.

Amit Daryanani - *RBC Capital Markets - Analyst*

Perfect. Thank you.

Operator

Jim Suva, Citi.

Jim Suva - *Citigroup - Analyst*

Thank you very much and congratulations to you and your team. The recent PMI data out of China has been above 50. Is that been in line with your expectations or better than expected? Because I believe that is one of the leading indicators you look at.

And then my follow-up question is, I assume that the oil pricing has a lot to do with the state of the heavy vehicles. Meaning the lower the oil price, then the less heavy equipment is being purchased to extract raw materials and oil and precious metals and such like that. What type of level do you look at for a reaccelerations in heavy machinery? Is it above $50? Above $45 per barrel? Or how should we think about those metrics? Thank you.

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

Sure Jim. On the PMI front, we look at the manufacturing component of that PMI in particular, and it's operating where we expect it to be. Our concern had been if we saw that move down, we would have anticipated another round of inventory cuts in China. And that said, it was not part of our thesis going forward. So, it's really playing out as expected.

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On the question of heavy truck, it's an interesting question. We have got two parts to our overall HVOR business. So, that now comprises about 15% of the revenue of Sensata. About half of that is off-road. And then you get into a lot of fragmentation in that off-road piece. So when you start to look at the piece of that that would be impacted by oil prices, it is a pretty small part of our overall off-road exposure, if you will. So we're not spending a ton of time looking at recovery in that particular area.

I think in general in the off-road part of the business, we're at least 18 months, 24 months to seeing meaningful recovery in things like agriculture. Construction probably comes in a little bit sooner and then there is a long line of tail beyond that, mining, and as you talked about, things that would relate directly to oil. So, a pretty small part of overall Sensata.

Jim Suva - *Citigroup - Analyst*

Got you. Can you just quickly update us on the timing for China tire pressure sensing regulations of A, when those kick into the general mandates over there? Plus, I guess more importantly, when do those start to impact Sensata? I would assume you build before it fully rolls out? When should we start to see meaningful traction and those regulations kick in?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

We think that the time of meaningful revenue, the mandate itself would be around early 2019. We do expect to see some pull ahead on that. Generally, we begin to see that adoption 12 months, 18 months ahead. That can be very economically influenced.

Not to get too long-winded here, but if you look at the Euro VI B ramp that we saw last year, that was regulation where OEMs waited until really the very last minute because it was a down market in Europe. That is not what we're thinking about in China, but those are some of the things that can swing whether the revenue comes sooner or whether it is really episodic.

Jim Suva - *Citigroup - Analyst*

Thank you and congratulations to you and your team at Sensata.

Operator

Shawn Harrison, Longbow Research.

Shawn Harrison - *Longbow Research - Analyst*

Hello. Good morning, everybody. I wanted you just check on the free cash flow forecast for the year. Did that change? I thought it was previously $350 million or $400 million, but the $102 million you did in the first quarter I think is an all-time record. So just any update on how you think about free cash flow for the year?

Paul Vasington - *Sensata Technologies Holding NV - CFO*

We're very excited about the cash flow in Q1, but it is pretty much in line with what we expected to occur. We're still going to hold to the $350 million to $400 million for the full-year, just given the volatility that can occur with things like receivables. I think we feel good about the $350 million to $400 million.

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Shawn Harrison - *Longbow Research - Analyst*

Is there any target exiting the year in terms of cash cycle days or improvement throughout the year?

Paul Vasington - *Sensata Technologies Holding NV - CFO*

Say that one more time.

Shawn Harrison - *Longbow Research - Analyst*

Cash cycle days. Are you targeting a certain number of decline in days for the year or just how you think about the cash cycle days for 2016?

Paul Vasington - *Sensata Technologies Holding NV - CFO*

At a high level, we continue to work inventory down. So days on hand should continue to improve. Receivables have been holding pretty steady with what we saw last year quarter by quarter. And we continue to work to improve our supplier terms on the payable side. So that should improve slightly over the course of the year.

Shawn Harrison - *Longbow Research - Analyst*

Okay. And as a brief follow-up, Martha, are you still forecasting auto production to be less than where industry forecasters are at right now? I know you had some concerns last quarter. And as a follow-up on auto as well, I think there was a comment within the presentation that you picked up some content in Europe and China. Maybe if you could just remind us what vehicle content is per region right now?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

I think relative to the market, yes, we are undercalling HIS on production in North America in particular. I think they may have lined up in Europe, but as we gave our guide, we were below their call at that time as well.

Relative to the content in Europe, it continues to be the highest point, the highest region for content in Sensata. We think that actually will start to change over time when we start to look at some of the things driving, for example, sensors due to onboard diagnostics. And sort of an embrace around the world on emissions enforcement under real world driving conditions. That is beginning to create content opportunities across the board in gasoline engines as well.

China remains the lowest for us. We are just under $10 of content in China. So it continues to be a really nice opportunity as we look ahead.

Shawn Harrison - *Longbow Research - Analyst*

Just to clarify. On annual production, are you still around 2% then internally baked into your forecast?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

That is right. Exactly.

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Shawn Harrison - *Longbow Research - Analyst*

Thank you so much.

Operator

Rich Kwas, Wells Fargo Securities.

Rich Kwas - *Wells Fargo Securities, LLC - Analyst*

Hello. Good morning, everyone. I just wanted to just on a follow-up on a question regarding regional production. Martha, are you in line with HIS now for Europe around 3% and then China, are you still expecting low single-digits for the year in terms of production growth?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

We are expecting low single-digits in China. We think we're seeing vehicle inventory build there in this quarter. So just despite probably production a little ahead of that in the first quarter, we're seeing vehicle inventory on that side. In overall Europe, we are at about a 2% look as we look ahead. Those are our --

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Rich Kwas - *Wells Fargo Securities, LLC - Analyst*

Okay. Thank you. And then on the PMI, with the government data above 50, should we assume that the guidance for the year assumes that PMI stays above 50 for the balance of the year? And what are the risks if it goes back below 50 in terms of your outlook for the year versus the solutions?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

From what we have seen, it is not a hard on/off switch, but that 50 point is important. It's one that whether we are in a recessionary mode or continue to be in a recessionary mode there or not. We think things stabilized at just below 50 in the past, where we haven't actually seen order rates drop off. And some of that is just understanding where we play, so making sure that you're looking at the manufacturing PMI in particular. But that level is an important consideration for us.

Rich Kwas - *Wells Fargo Securities, LLC - Analyst*

Last one for me in longer-term. With regards to the business wins you announced in aerospace and with the chiller win, when does that start to come online? How far out are we from that?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

Aerospace is long cycle. It is pretty similar to auto, if not longer. We're three years or four years out before that actually hits. Cycle on the industrial side a little bit shorter. More 18 months to 24 months, so those wins begin to play out for us on top line.

Rich Kwas - *Wells Fargo Securities, LLC - Analyst*

Okay. Great. Thank you.

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Operator

William Stein, SunTrust.

William Stein - *SunTrust Robinson Humphrey - Analyst*

Hello, thank you for taking my question. I'm hoping you can talk a bit about a topic that hasn't been as prominent in the news lately, this VW emissions scandal and echoes of that seem to potentially be coming from some of the other OEs. What is the current status of any impact on Sensata's business from that and longer-term, do anticipate this to be a net positive or negative for the business?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

On Volkswagen, we had talked about $8 million to $10 million in revenue in the US that would be impacted this year. That was our guide, Will. And that's just vehicles that are not going to be sold on the US market. So those are some of the very analytical puts and takes on that.

When you look at what is happening now in the minds of regulators and with customers, this notion again, of not just having vehicles perform cleanly at launch or through submitted information, but enforcing on it in the field and on an ongoing basis, we think it is a very important development. We believe that it is an upside for Sensata and we're having conversations right now about the sensor content that is demanded as you begin to look at ways of making sure your vehicle does not drift in terms of performance over time. So it is a net positive for Sensata.

William Stein - *SunTrust Robinson Humphrey - Analyst*

One more if I can. I apologize. I joined late, so if you already addressed this. Last quarter, there was an initial discussion about the Company's position in all electric vehicles. I'm wondering if you can update us on that? It is great to see the Company move into these other areas of automotive like the ADAS investment and Quanergy. But I'm wondering if you can talk about the all electric vehicle and whether there is any incremental position there for the Company?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

Just to reiterate what we talked about last time around. What we are seeing is the notion of the range of these vehicles becomes a really important competitive differentiator for all electric vehicles. So when you look at what those OEMs are willing to do in those platforms to extend the range, we're seeing a lot more opportunity honestly, than we expected in these subsystems.

So we get to the point now where the content opportunity available to us is very similar on an all electric vehicle compared to a standard overall gas engine. We talked about things like $30 of content on some very specific makes and we continue to work those opportunities. So it is a development that's certainly interesting. We're getting pretty agnostic as to how the world actually plays out on that front because we have the content opportunity.

William Stein - *SunTrust Robinson Humphrey - Analyst*

That is very helpful. Thank you.

Operator

Samik Chatterjee, JPMorgan.

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Samik Chatterjee - *JPMorgan - Analyst*

Hello. I just had a question on CST and I appreciate all your comments today about the new business win there. But I think in the past, you mentioned that you wouldn't see a lot of growth in our business because of the lack of investment for growth on the previous ownership. So maybe if you can share your thoughts about how long do think it takes to build a pipeline there were CST will grow at the level that you think it has the potential to grow at?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

Sure. We think it is a two-year to three-year time horizon. And that's why getting on the ground and getting those wins underway right now is important because they are long cycle, Samik. So that is part of the thinking here.

Samik Chatterjee - *JPMorgan - Analyst*

Okay. Great. And just the second question I just wanted to check. Your leverage guidance for the end of the year does indicate you would be pretty focused on paying down debt. But there going to set off (inaudible) talks on the balance of buybacks versus leverage and how you are thinking about that as you go through the year?

Paul Vasington - *Sensata Technologies Holding NV - CFO*

The leverage ratio coming down is a combination of debt repayment and growing our EBITDA. And as we stated before, we take a balanced approach, a holistic approach, to how we deploy capital considering share purchases that were payment in M&A.

Samik Chatterjee - *JPMorgan - Analyst*

Okay. Great, thank you.

Operator

Jeremy Ketron, CLSA.

Jeremy Ketron - *CLSA - Analyst*

Thank you. Good morning, everyone. I just wanted to go back to the sensing solutions margins. Pretty impressive expansion here year-over-year despite the contraction in the business there. I wonder if you could unpack this margin expansion? I suppose the integration of CST is playing a role in here as well, but just some more color here is appreciated. Thanks.

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

It is primarily driven by our core business on sensing solutions. With the recognition that a portion of that business was not going to enjoy secular top line growth, there is I would say a really redoubling of effort on efficiencies, on ways to create earnings potential to make sure that it is performing on the bottom line similar to Sensata. Paul, I don't know if you have anything to add to that.

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Paul Vasington - *Sensata Technologies Holding NV - CFO*

Over the course of the last 6 months to 9 months, we've been taking steps to restructure our cost structure to drive that kind of profitability margin expansion.

Jeremy Ketron - *CLSA - Analyst*

So how do we think of the trajectory through the remainder of the year as you integrate CST as opposed to more spending on the front?

Martha Sullivan - *Sensata Technologies Holding NV - President & CEO*

I think the challenge in answering that question is that we will continue to look for opportunities to accelerate the integration. And that's could have us increasing integration spend or reducing spend quarter to quarter. So it is one of the reasons we're not necessarily guiding on our overall segments. We expect the profitability to, absent integration, to maintain its overall performance.

Jeremy Ketron - *CLSA - Analyst*

Understood. And Paul, a question on ForEx, the negative impact for this year is $0.17 to $0.21. It seems to be up a little bit from the trial guidance and so explain to us the dynamics there and how do we think about the headwind going to 2017 as the hedges roll off?

Paul Vasington - *Sensata Technologies Holding NV - CFO*

$0.17 to $0.21 is the guidance that we established at the beginning of the year, so that remains consistent. The first quarter of the four quarters, will have the lowest impact because the value that hedges that were in place were more valuable in the first quarter. Those will be behind us and as we get into the rest of the year, the value of those hedges become less. So the EPS impact will be bigger in the second, third and fourth quarter.

As we look to 2017, the $0.17 impact from our foreign exchange appears to look similar to what we saw in 2015, which was about $0.03 to $0.05. But that will change over time as exchange rates move and our hedges are put in place. That seems about a fair range.

Jeremy Ketron - *CLSA - Analyst*

Thank you.

Operator

There are no further questions at this time. I will turn the call back over to the presenters.

Jacob Sayer - *Sensata Technologies Holding NV - VP of Treasury and IR*

Thanks, Keith. I'd like to thank you all for joining our first quarter 2016 financial results call today. Later in the quarter, Sensata will be participating in Oppenheimer's Technology Investor Conference in New York on May 10, and Bank of America Merrill Lynch's Tech Investor Conference in San Francisco on June 1. We appreciate your continued interest and support of Sensata and look forward to speaking with you on the road and again, next quarter. Thank you and goodbye.

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Operator

Ladies and gentlemen, this concludes our program for today. You may now disconnect and have a wonderful day.

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