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CORPORATE PARTICIPANTS

Joshua S. Young *Sensata Technologies Holding PLC - VP of IR*

Martha N. Sullivan *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Paul S. Vasington *Sensata Technologies Holding PLC - CFO, CAO & Executive VP*

CONFERENCE CALL PARTICIPANTS

Amit Jawaharlaz Daryanani *RBC Capital Markets, LLC, Research Division - Analyst*

Brian Arthur Johnson *Barclays Bank PLC, Research Division - MD & Senior Equity Analyst*

Christopher D. Glynn *Oppenheimer & Co. Inc., Research Division - MD and Senior Analyst*

Craig Matthew Hettenbach *Morgan Stanley, Research Division - VP*

Jim Suva *Citigroup Inc, Research Division - Director*

Joseph Craig Giordano *Cowen and Company, LLC, Research Division - MD and Senior Analyst*

Mark Trevor Delaney *Goldman Sachs Group Inc., Research Division - Equity Analyst*

Matthew John Sheerin *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Senior Equity Research Analyst*

Richard Michael Kwas *Wells Fargo Securities, LLC, Research Division - MD & Senior Equity Research Analyst*

Samik Chatterjee *JP Morgan Chase & Co, Research Division - Analyst*

Shawn Matthew Harrison *Longbow Research LLC - Senior Research Analyst*

Steven Bryant Fox *Cross Research LLC - MD*

Wamsi Mohan *BofA Merrill Lynch, Research Division - Director*

William Stein *SunTrust Robinson Humphrey, Inc., Research Division - MD*

PRESENTATION

Operator

Good day, and welcome to the Sensata Technologies Second Quarter 2018 Earnings Call. (Operator Instructions) Please note this event is being recorded. I would now like to turn the conference over to Mr. Joshua Young, Vice President, Investor Relations. Please go ahead, sir.

Joshua S. Young - *Sensata Technologies Holding PLC - VP of IR*

Thank you very much, Laura, and good morning, everybody. I'd like to welcome you to Sensata's Second Quarter 2018 Earnings Conference Call. Joining me on today's call are Martha Sullivan, Sensata's President and CEO; and Paul Vasington, Sensata's Chief Financial Officer.

In addition to the earnings release we issued earlier today, we will be referencing a slide presentation during today's conference call. The PDF of this presentation can be downloaded from Sensata's Investor Relations website. And we will also post a replay of today's webcast shortly after conclusion of today's call.

Before we begin, I'd like to reference Sensata's safe harbor statement on Slide #2. During the course of this conference call, we will make forward-looking statements regarding future events or the financial performance of the company that involve certain risks and uncertainties. The company's actual results may differ materially from the projections described in such statements. Factors that might cause such differences include, but are not limited to, those discussed in our Forms 10-Q and 10-K as well as other subsequent filings with the SEC.

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On Slide #3, we show Sensata's GAAP results for the second quarter of 2018. We encourage you to review our GAAP financial statements in addition to today's presentation. Most of the subsequent information we will discuss during today's call will be related to non-GAAP financial measures. Reconciliations of our GAAP to non-GAAP financial measures are included in our earnings release and in our webcast presentation. Additionally, the company provides details of its segment performance on Slides 10 and 11, which are the primary measures management uses to evaluate the business.

Martha will begin today's call with an overall business summary. Paul will then cover our financials for the second quarter of 2018 and provide guidance for the third quarter as well as update our full year 2018 guidance. We then take your questions after our prepared remarks.

Now I'd like to turn the call over to Sensata's President and CEO, Martha Sullivan.

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Thank you, Joshua, and thanks to everyone on the call for joining us this morning. Sensata is continuing to deliver on the expectations we've set with investors. We had a strong second quarter, building on our solid performance in Q1 to generate excellent operating results in the first half of 2018. We are accelerating our organic revenue growth, expanding our margins, generating mid- to high-teens EPS growth and delivering on our promise to bring more balance to our capital deployment program.

For the second quarter, we reported revenues of $913.9 million and exceeded the high end of our guidance for organic revenue growth. We expanded our adjusted EBIT margins organically by 100 basis points year-over-year and delivered adjusted EPS of $0.93, which represents 15% organic growth over the second quarter of last year.

On Slide 4, I go into more detail and list some of the key highlights of the second quarter. I want to remind investors that Sensata is a leading industrial technology company with secular growth opportunities across multiple end markets. You've heard me talk in the past about how we have strategically increased our exposure to markets, such as HVOR, industrial and aerospace, that offer compelling content growth opportunities.

Over the past 5 years, our revenue exposure to automotive has dropped approximately 10 percentage points. Our non-auto markets drove strong growth in 2017 and were the primary drivers of our 6.4% organic revenue growth in the second quarter this year. All of our businesses, including our auto business, outgrew their underlying markets in the second quarter. This helped us to increase our organic revenue growth rate by 280 basis points compared to the prior year quarter.

Next, we are continuing to generate robust adjusted EBIT margin expansion. We expanded our adjusted EBIT margins by 40 basis points in the second quarter of 2018. On an organic basis, adjusted EBIT margins expanded by 100 basis points. This is our sixth straight quarter of delivering EBIT margin expansion. On the bottom line, we continue to deliver double-digit EPS growth. We reported 15% growth in adjusted earnings per share as a result of higher volume, acquisition cost synergies and lower integration costs.

At the end of May, we finished an intense 18-month process to redomicile the company to the U.K. With the redomicile complete, we now have the ability to repurchase our shares. As a result, the board put in place a $400 million stock repurchase authorization in early June. During the second quarter, we repurchased 1.1 million shares for a total consideration of $60 million. We anticipate using up the $400 million authorization within the next 6 months, at which point we expect to attain another repurchase authorization from our board.

Slide 5 shows organic revenue growth by end market in the second quarter. Beginning with HVOR, which generated 14.3% organic revenue growth in the quarter. HVOR serves a number of submarkets, including the on-road truck, construction, agriculture, marine and recreational vehicle market. All of these segments are posting strong secular growth, which enabled HVOR to outgrow its market organically by 660 basis points in the quarter. It is important to point out that this secular growth is sustainable, and we have good visibility into our future content growth due to the long-cycle nature of our business model.

Regardless of where we are in the market cycle, you can expect Sensata to consistently outperform underlying production. Additionally, I'd point out that the market for HVOR continues to strengthen. We now expect end market growth for HVOR to be between 7% to 8% for the full year,

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which is above our previous guide. One of the exciting developments in the quarter was that we closed our first win for a new steer-by-wire application in HVOR. Steer-by-wire is a fundamental building block to enable autonomy in HVOR. This early win is proof of the value we can bring in autonomy for the HVOR market.

Next, I want to turn to industrial, aerospace and other end markets, which are served by our Sensing Solutions segment and represent approximately 25% of Sensata's total revenues. For the second quarter of 2018, we generated 7.6% organic revenue growth, a very strong result for this business. We expanded our industrials business through the CST acquisition. And when we did that, we saw strong growth potential in a number of industrial markets. And you are now seeing this growth manifest itself in the higher-growth profile of Sensing Solutions.

One of the ways we are driving this growth is by leveraging cross-selling opportunities since many of our customers have the potential to buy both our control and sensor products. From a geographic perspective, our North American and Asian businesses were once again the strongest performers. In addition, we generated solid growth in our aerospace business as industry fundamentals of this long-cycle business remain healthy and a number of new airplane models are launching. Going forward, Sensing Solutions is poised to have another strong year.

Finally, our automotive business outgrew its market and posted 3.9% organic revenue growth. Through the first 6 months of the year, our auto business has outgrown the market by 330 basis points. China continues to be the primary driver of strength for auto as content per vehicle continues to rise rapidly as a result of modernization and new legislation. North America also had a solid quarter of growth despite the fact that the market continued to decline. This was a result of growing content on cleaner, more efficient vehicles. Finally, we continue to secure new sensor content wins on gas engines in Europe, even as the diesel decline accelerates.

On Slide 6, I show a slide that we first shared at our Investor Day. There are 3 key drivers of our growth between now and 2020: first, the constant need for cleaner and more efficient transportation and equipment; second, the growing mandate for electrified products in auto as well as other end market; and third, the modernization of auto and industrial equipment in China as well as new regulation for cleaner and more efficient products.

Since the beginning of 2018, we have made important progress in all of these areas, ranging from new wins for next-generation gas powertrains to robust performance in China, where we have generated very strong double-digit organic revenue growth through the first 6 months of this year. For electrification, I want to stress that while we are working on longer-term innovations, we are also winning wins -- we are also seeing wins and new revenue today. This applies to areas such as thermal management but also to applications such as regenerative braking, which I will discuss in further detail on Slide 7.

On Slide 7, I show an example of where Sensata is gaining content today on electric vehicles. Electrification is a net content tailwind for our automotive business, and over the long term, offers a tremendous opportunity for Sensata. One example of this is regenerative braking, which is a requirement for nearly all electric and hybrid vehicles in order to improve efficiency and optimize the performance and range of the battery. It works by using electric motor braking torque to slow the vehicle until standard friction braking force is required.

On average, regenerative braking systems will add at least 1 additional sensor with some customers adding as many as 5 sensors to the system. Additionally, installation rates for regenerative braking are very low today. As volumes of hybrid and electric vehicles ramp, Sensata will experience nice content growth on these systems. I share this with you as a clear example of where our core sensor content is expanding on electrified vehicles and to stress that we are winning business and recognizing revenues from these applications today.

I want to wrap up the presentation by reviewing our first half performance against the operational goals and long-term guidance we laid out at our Investor Day. These are explicit metrics which investors can use to measure our progress. In the first half of 2018, we have demonstrated solid execution against each of these priorities.

We are accelerating our growth, delivering 6.4% organic revenue growth on a year-to-date basis, which is above the high end of our 3-year CAGR of 4% to 6%. We are increasing our margins, expanding our adjusted EBIT margin by 110 basis points organically. We are delivering double-digit bottom line growth, posting 15.8% growth in adjusted EPS versus our long-term guidance of 10% to 13%. And we have increased our flexibility

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for value-creating capital deployment by completing our redomicile to the U.K. and putting in place a $400 million share repurchase program. We have already repurchased $60 million of stock in Q2. And we expect to use up the remaining authorization within the next 6 months.

So as you can see, our entire management team is focused on attaining our goals and 3-year financial targets. And we are off to a great start delivering on these promises to shareholders. I'd now like to turn the call over to Paul to review our second quarter results in more detail and to provide financial guidance for the third quarter and update guidance for the full year 2018. Paul?

Paul S. Vasington - *Sensata Technologies Holding PLC - CFO, CAO & Executive VP*

Thank you, Martha. Key highlights for the second quarter, as shown on Slide 9, include revenue of $913.9 million in the quarter, an increase of 8.8% from the second quarter of 2017. Of this growth, changes in foreign currency increased revenue by 2.4%. The net result was 6.4% organic revenue growth in the quarter.

Adjusted EBIT was $210.4 million in the quarter and grew 11% compared to the second quarter of 2017 or 11.1% on an organic basis. Adjusted EBIT margins were 23% of revenue in the quarter and increased 40 basis points compared to the second quarter of 2017 or 100 basis points on an organic basis.

Adjusted net income was $160.8 million in the quarter and grew 15.7% compared to the second quarter of 2017 or 15.8% on an organic basis. Adjusted net income margins were 17.6% of revenue or an increase of 100 basis points compared to the second quarter of 2017 or 140 basis points on an organic basis. Adjusted EPS was $0.93 in the second quarter of 2018, a $0.12 increase from the prior year quarter, primarily due to higher volume, productivity gains, acquisition cost synergies and lower integration spend.

Changes in foreign currency had a negligible year-over-year effect on our performance in the quarter. That being said, the impact of foreign currency on adjusted EPS was $0.05 lower in the second quarter of 2018 than our previous guidance. And I'll provide more details about this later in the presentation. Despite the lower-than-expected contribution from foreign currency, we exceeded the midpoint of our EPS guidance through stronger underlying operating performance.

Now I'd like to comment on our 2 business segments. And I'll start with Performance Sensing on Slide 10. Our Performance Sensing business reported revenues of $676.2 million for the second quarter of 2018, an increase of 8.7% compared to the second quarter of 2017 or 5.9% organic revenue growth for the same period. The heavy vehicle and off-road business, which reported organic revenue growth of 14.3% in the second quarter of 2018, continues to have the strongest revenue growth in this segment as all of its markets remain very strong. Our automotive business reported organic revenue growth of 3.9% in the second quarter of 2018, outpacing the market and led by China, which posted another quarter of strong double-digit organic revenue growth as our content per vehicle steadily rises as expected in the region.

Performance Sensing profit was $187.4 million or 27.7% of revenue for the second quarter of 2018. Excluding the impact of foreign currency, Performance Sensing profit as a percentage of revenue was 27%, down 20 basis points from the year-ago quarter as a result of increasing R&D effort to execute new design wins and fund development activities to intersect emerging mega trends that are shaping our markets, partly offset by acquisition cost synergies.

As shown on Slide 11, Sensing Solutions reported revenues of $237.6 million in the second quarter 2018, an increase of 9% compared to the second quarter of 2017 or 7.6% organic revenue growth for the same period, reflecting strong demand from our customers in China and North America as well as high single-digit organic growth from our aerospace business.

Sensing Solutions profit was $79.1 million in the second quarter 2018, an increase of 12.8% from the same quarter last year. Excluding the impact of foreign currency, Sensing Solutions profit as a percentage of revenue was 32.7%, a 60 basis point increase year-over-year, resulting from net productivity gains on higher volume, acquisition cost synergies and lower integration spend.

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Corporate and other costs, not included in segment operating income, were $53.5 million in the second quarter of 2018, up approximately $1.7 million year-over-year due to unfavorable movements in foreign currency and higher compensation costs. Excluding charges added back to our non-GAAP results, corporate and other costs were $46.7 million in the second quarter of 2018.

Slide 12 shows Sensata's second quarter 2018 non-GAAP results. Adjusted gross profit increased 10.1% year-over-year to $335.7 million. Adjusted gross profit margins were 36.7%, up 40 basis points versus the same period in the prior year. A higher R&D spending this quarter reflects increased design and development effort to execute new design wins as well as fund development activities to intersect emerging mega trends that are shaping our market, such as electrification, autonomy and smart connected. Restructuring and amortization expenses reflect lower year-over-year integration costs in the second quarter of 2018.

Adjusted other loss net of $7.9 million is primarily comprised of foreign currency losses resulting from the devaluation of net monetary assets denominated in Chinese renminbi. The adjusted tax rate was 6.2% in the second quarter of 2018, 30 basis points lower than the prior year quarter. And for the full year, we are maintaining our adjusted cash tax rate target of 7%. On the bottom line, adjusted net income margins improved by 100 basis points and adjusted EPS increased by 14.8% in the second quarter of 2018 as compared to the prior year quarter.

Moving to Slide 13. Sensata generated strong operating performance in the second quarter of 2018, which more than offset a $0.05 lower-than-expected EPS contribution from foreign currency as compared to the guidance we provided in April. This slide is meant to help investors understand how foreign currency impacted Sensata's P&L and how our cash flow and balance sheet hedging affects our bottom line results.

The table on Slide 13 depicts the financial impact that changes in foreign currency had on our income statement in both the second quarter of 2018 and on a year-to-date basis. As you can see, foreign currency increased our revenues considerably in the first 6 months of the year but has very little impact on our adjusted EPS, adding only $0.02 of earnings. Included in this small EPS impact are the hedges we put in place to reduce near-term earnings volatility.

In the line item adjusted other net just below profit from operations on this slide, you can see the unfavorable impact changes in foreign currency had on our balance sheet net of hedges. The main contributor to the unfavorable second quarter result in adjusted other net was a 5% depreciation of the Chinese renminbi, which was the highest level of depreciation the currency has seen over the past 2 years. This loss in Q2 was unusual.

Also we are reducing our China cash that is denominated in Chinese renminbi by about 50% to further reduce earnings volatility related to this currency. For the full year 2018, we expect foreign currency will have a $0.05 to $0.09 favorable impact on adjusted EPS. And looking forward to 2019, we expect foreign currency will provide about a $0.10 year-over-year favorable adjusted EPS benefit based on current rates and exposures.

On Slide 14, I show our financial guidance for the third quarter of 2018. Overall, we expect to report revenues between $851 million and $875 million, representing reported revenue growth of 4% to 7%. At the midpoint of our guidance, we expect that foreign currency will increase revenues year-over-year by approximately $2 million in the third quarter of 2018. Excluding the effect of foreign currency, we expect to report organic revenue growth of 5% to 7% in the third quarter of 2018.

Our current fill rate is approximately 85% of the revenue guidance midpoint for the third quarter of 2018. We expect to report adjusted EBIT between $201 million and $207 million, which would represent organic growth of 6% to 7%. On the bottom line, we expect to report adjusted net income between $150 million and $156 million and adjusted EPS between $0.88 and $0.92, which would represent organic growth of 9% to 11%. Changes in foreign currency are expected to increase adjusted EPS by approximately $0.01 to $0.03.

Now let me turn to our guidance for the full year 2018 as shown on Slide 15. Based on the strong results for the first 6 months of the year, we are increasing our guidance for organic revenues and adjusted EPS. We expect revenues to be in the range of $3.493 billion to $3.555 billion for the full year 2018, a 6% to 8% increase on a reported basis. We expect foreign currency to increase our revenues by 1% to 2%.

Excluding foreign currency and the impact of our expected valves divestiture, we expect organic revenue growth of 5% to 7%, which is up considerably from our previous guidance of 3% to 5%. We expect adjusted EBIT between $821 million and $837 million, which would represent organic growth of 9% to 11%. On the bottom line, we expect adjusted net income between $618 million and [$634 million] (corrected by company

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after the call) and adjusted earnings per share between $3.63 and $3.73 for the full year 2018, which would represent organic growth of 14% to 15% compared to our previous guidance of 9% to 13%.

Our adjusted EPS guidance for the remainder of the year includes: the effect of divesting our valves business during the third quarter of 2018; increased investment in the businesses for higher revenue growth; and the near-term impact from recently enacted [Section 301 China tariffs] (corrected by company after the call), which we expect to offset by the time we enter 2019. We expect to generate free cash flow between $522 million and $543 million in 2018, which assumes capital expenditures of approximately $150 million to $160 million. Our guidance assumes no M&A and that we will complete our current $400 million share repurchase authorization within the next 6 months.

I will conclude my remarks with Sensata's investment summary on Slide 16. Sensata is a leader in the opportunity-rich sensing market, where we provide differentiated sensing solutions for mission-critical applications. When we combine these solutions with our low-cost global supply chain, we deliver industry-leading margins, strong free cash flow and consistent double-digit adjusted earnings per share growth. As you've seen again this quarter, our revenue growth is accelerating and we are well positioned to benefit from growing industry mega trends.

We consistently produce industry-leading margins that continue to expand due to our organizational discipline. Further, we have demonstrated a strong track record of producing double-digit organic adjusted EPS growth. With a strong balance sheet, attractive free cash flow generation and balanced value-creating capital deployment, including our recent $400 million share repurchase program, we are in an excellent position to provide attractive returns for our shareholders. This is an exciting time for Sensata and we believe we offer compelling investment opportunity for investors.

Now I'd like to turn it back over to Joshua.

Joshua S. Young - *Sensata Technologies Holding PLC - VP of IR*

Thank you. Laura, please assemble the Q&A roster.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question will come from Christopher Glynn of Oppenheimer.

Christopher D. Glynn - *Oppenheimer & Co. Inc., Research Division - MD and Senior Analyst*

So just looking at the ramp in R&D, I think, as expected, maybe a little more. But just wondering how that is kind of playing into your confidence in the 2019 organic continuity, the direct or indirect correlation there and how you see R&D trending over the next year-plus.

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Yes, Chris, there is a correlation there that really underpins our 3-year guide if you look at what we're seeing between now and 2020 and is evidence of our confidence in what we're going to deliver there. There are also elements of that, that are focused beyond 2020, when we look at our overall opportunity and some really growthful trends around electrification, for example, and smart and connected opportunities in our industrial landscape. So when we think about that, we think the index coming out of the year is appropriate. We'll continue to take a look at that. Part of that investment can -- also impacts just pull-in on product launches. So that again underpins our confidence in our overall organic growth guide.

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Christopher D. Glynn - *Oppenheimer & Co. Inc., Research Division - MD and Senior Analyst*

Great. And then on China EV, I'm wondering how you're thinking about prospects for that market to break ahead of forecast. I think there's been some step-up and emphasis on the infrastructure over there.

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Yes. We watch that really closely. And so when we look at projections, and everybody has their point of view on this, one of the sensitivities around our model is infrastructure. So what we see happening in China is really playing out along with the assumptions that we put in place because many of the initiatives there were described by (inaudible) in their overall China 2025 initiative, so playing out the way we called it.

Operator

The next question comes from Samik Chatterjee of JPMorgan.

Samik Chatterjee - *JP Morgan Chase & Co, Research Division - Analyst*

The first thing I wanted to check on is you mentioned in the remarks that you expect Sensing Solutions to have a strong year. But if you could talk about how the organic growth, which is high single digits now this year, how is that tracking relative to your expectations at the start of the year? And which kind of pockets are where you're seeing the strength here? And what's sort of driving the confidence in maintaining that kind of high single-digit growth in that business?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

So you've seen us raise our overall revenue guide for the year. And the performance in our industrial market is one of the key factors there. So our confidence remains quite high. When we look at what's driving that, it really is lined up with the themes that we've talked about are driving overall Sensata. So China, very important element. What we see happening in China is the modernization of industrial equipment, the move to variable control for better efficiency. We're playing strongly in those opportunities. The other thing I would point out is electrification. So beyond auto, where we all think about that, we're actually seeing elements of things like power tools now move to be electrified. And that plays really nicely to our electrical protection portfolio that we have. And then thirdly, I'd point out when we made the acquisition with CST, that was a business that had nice technology but wasn't growing. And we've been able to bring more share of wallet to our industrial customers as a result of that acquisition. And we now see that playing out in our growth rate. So those are some of the things that underpin our confidence.

Samik Chatterjee - *JP Morgan Chase & Co, Research Division - Analyst*

Got it. And then on the HVOR market, you mentioned the first award for the steer-by-wire applications. Can you give us a sense of what is a typical time to market for such product after the award win and what kind of content per vehicle would that sort of result in?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Yes, we would expect to be launching that within the 2, 2.5-year time horizon. So this one is a little bit shorter cycle. This is a system-level solution. So when you think about the ASP here, we're talking [as much as $900 of content] (corrected by company after the call). Obviously, a smaller volume base when you look at the construction market, but it's a meaningful part of our growth rate going forward.

Operator

Our next question comes from Shawn Harrison of Longbow Research.

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Shawn Matthew Harrison - *Longbow Research LLC - Senior Research Analyst*

Wanted to delve into the tariff situation on a couple fronts. Paul, you mentioned, I guess, some cost headwinds associated with that. But if you could also talk about whether you need to move any of your production globally or that's being considered? Or are you seeing any demand disruption issues as well just from the broader tariff situation?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Yes. So just as a reminder, and thanks for the question, we have a really cost-effective global supply chain footprint. But given that we're often sole-sourced, we have a lot of redundancies in that footprint. So for our key products, we make those in multiple locations. We've been really proactive on this [code 301 issue] (corrected by company after the call), so began working with customers long before it was implemented to look at the flow of our products to those customers. And that's the reason why we're really confident that this is behind us as we exit 2018.

Shawn Matthew Harrison - *Longbow Research LLC - Senior Research Analyst*

Is there a way to put the kind of the cost you're facing now kind of basis points or dollars or (inaudible)?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Yes, sure, yes. We expect in 2018, for the second half of the year, for that to range between $6 million to $8 million. So that is a bit of a headwind in 2018. And despite that, you've seen where we've landed in our guide.

Shawn Matthew Harrison - *Longbow Research LLC - Senior Research Analyst*

Perfect. And then just a brief follow-up, the valves divestiture, I'm assuming that's now backed out of the guidance for the fourth quarter. If I'm correct, it was $117 million of annual sales and about $0.10 of EPS. Is that the right range to kind of size that business?

Paul S. Vasington - *Sensata Technologies Holding PLC - CFO, CAO & Executive VP*

That's correct. We've taken it out of the guide, assuming a close in the third quarter. So revenue and profit have been adjusted accordingly.

Operator

The next question comes from Amit Daryanani of RBC Capital Markets.

Amit Jawaharlaz Daryanani - *RBC Capital Markets, LLC, Research Division - Analyst*

I guess, first one, nice to see the data on the regenerative braking content in EV from you guys. Could you just talk about on a broader basis though, what is the content per vehicle in EV versus a traditional combustion engine? And is your market share importantly any different in the market today versus what it (inaudible)?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

I think we lost you at the end of that question. But I think I know what you were getting at there. So the way we've been looking at this because the EV market is still quite small and quite fragmented, but when we look at where volume is building around key models, so think models that

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have more than 20,000 units of volume, we're now at the point where that content is equivalent to our conventional content. And we see that growing as more of these systems get efficient. So to give you a sense of it, that can -- ranges to a high of about $50 per vehicle. And in that same range, we have some that are more in the mid-20s. But if you look at the overall average, it's right in line with our current content today on ICE engines.

Amit Jawaharlaz Daryanani - *RBC Capital Markets, LLC, Research Division - Analyst*

Perfect, that's very helpful. And then I guess, Martha, just on the HVOR market, I think you're raising the underlying unit expectations for 2018. Do you see unit growth sustaining in 2019 as well? Because some of the Class 8 trucks, for example, it seems like '18 is not big, it might be more like a '19. So just wondering from a unit basis, do you see that growth sustaining in '19 as well?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

From an end market point, meaning independent of our secular growth in that the segment, which as you know is quite a strong, no, we would not expect the end market to expand from '18 to '19. The question is where is the peak in that overall cycle. I think one thing to keep in mind, that the probably most volatile piece of that is the Class 8. And I think that's what you're asking about. That's only 15% of our revenues in HVOR. So that being said, it's really the Class 8 piece that we would not expect to see expand as we go from '18 to '19. In some of the other segments, particularly those in Europe and elements of the off-road market, we do see some more end market expansion, although that's not really what's driving most of our growth.

Operator

(Operator Instructions) And our next question will come from Wamsi Mohan of Bank of America Merrill Lynch.

Wamsi Mohan - *BofA Merrill Lynch, Research Division - Director*

So when we look at the auto business, you had 5 to 6 points of delta versus end market growth in 1Q. But you only have 1 point ahead of end market growth in the second quarter. Just wondering what contributed to that change. And how much in excess of end market growth do you expect for the full year?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Yes, so what drives our growth in auto, given that we're not expecting or not seeing much end market help at all from a production perspective, it is our content growth. And that content comes in with new product launches, which does not happen in a linear way throughout the year. So it's not unusual for us to see stronger content growth. Some of that subside quarter-to-quarter. Through the first half of the year, we're operating now at about 4.2% overall organic. We expect the second half in auto is actually going to be stronger in terms of our content performance, just given what we know is launching in the second half of the year. And we expect to perform right in line with our overall organic CAGR guide for all of Sensata.

Wamsi Mohan - *BofA Merrill Lynch, Research Division - Director*

And as a follow-up, in Performance Sensing on an organic basis ex currency, margins declined slightly. I know Paul called out some investments that were an offset. Can you unpack that for us a little bit? How much benefit did you actually see in the underlying margins before those investments? Or if you could size the incremental investments that you're making for the new design opportunities, that would be helpful.

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Paul S. Vasington - *Sensata Technologies Holding PLC - CFO, CAO & Executive VP*

Yes, I would say that higher investment from R&D was about a 60 basis point headwind. And the synergies that we are generating negated that. And then it's our normal productivity gains that we see in that business that we get on a consistent basis, which can be lumpy though quarter-to-quarter.

Wamsi Mohan - *BofA Merrill Lynch, Research Division - Director*

All right. And then if I could, one last one. You actually managed to keep the full year midpoint of guidance unchanged despite both the headwinds from the divestiture of the valves business and the lower FX tailwinds. And offsetting this is your higher organic growth. So what has changed in the past 90 days that gives you this confidence of 2 point better organic growth? Where's that incremental growth really coming from? It seems like it's going to be mostly a Q4 phenomena. And how much of that is really HVOR, which you noted is clearly doing better?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Look, the nature of our business is we've got good visibility into the overall backlog. We know what's launching and ramping in the second half of the year. We've sized the headwinds that you talked about. So we're managing those quite well. And that really is what gives us the confidence to look ahead and provide the guide that we provided.

Paul S. Vasington - *Sensata Technologies Holding PLC - CFO, CAO & Executive VP*

And Wamsi, we have about 6% growth in Q3. So it is continued strength throughout the second half, not just the fourth quarter.

Operator

The next question will come from Rich Kwas of Wells Fargo.

Richard Michael Kwas - *Wells Fargo Securities, LLC, Research Division - MD & Senior Equity Research Analyst*

Martha, on diesel, so I think 39% is the level for 2020. It seems like in Europe, that's coming in below, so you have some offsets. Can you just go into some detail as we think about '19 and '20 in terms of the organic revenue growth, the offsets against some of the diesel trends?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Yes, it's increasingly moving in a one-for-one way, Rich. So the way to think about that is when the diesel comes down, what's backfilling that? And our content growth and what's backfilling that on gas engines is really growing. It actually grows more strongly in '19 than '18. So you've seen us be able to offset that overall impact as we move through the year. We've got really high confidence of that as we go forward and are recognizing, as you point out, that, that decline is happening more quickly.

Richard Michael Kwas - *Wells Fargo Securities, LLC, Research Division - MD & Senior Equity Research Analyst*

Right, okay. So it's gas engine. And then the content there is comparable at this point to diesel CPV or getting close?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

It's very close. And we outweigh as we go forward.

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Richard Michael Kwas - *Wells Fargo Securities, LLC, Research Division - MD & Senior Equity Research Analyst*

Okay. And then just a couple for Paul. So 301, China Section 301, is that incorporated into this headwind for the balance of the year as well?

Paul S. Vasington - *Sensata Technologies Holding PLC - CFO, CAO & Executive VP*

Yes, we're not impacted by that. 301 doesn't impact us, no.

Richard Michael Kwas - *Wells Fargo Securities, LLC, Research Division - MD & Senior Equity Research Analyst*

Not at all, okay, No effect, okay. And then just with the fill rate at 85%, as you look at China right now, what are you seeing? Any changes in demand trends versus the first half of the year that would be noteworthy either way?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

No, we're not seeing that subside at all. So that's developing as expected.

Operator

And the next question will come from Joe Giordano of Cowen.

Joseph Craig Giordano - *Cowen and Company, LLC, Research Division - MD and Senior Analyst*

So first of all, are you guys still using 0% as your global production estimate for the full year for your customers?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Are you asking about auto in particular?

Joseph Craig Giordano - *Cowen and Company, LLC, Research Division - MD and Senior Analyst*

Yes. Sorry, yes, auto in particular.

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Yes, we're between 0% and 1% for the full year.

Joseph Craig Giordano - *Cowen and Company, LLC, Research Division - MD and Senior Analyst*

Okay. And I think someone else said -- did you mention what the outgrowth was versus your adjusted production for your customers in this quarter? Because I know we went from 5 60 to 3 30 on the 6 months, so...

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Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

We actually put that in our press release. So it's about just under 110 basis points, something along those lines.

Joseph Craig Giordano - *Cowen and Company, LLC, Research Division - MD and Senior Analyst*

Okay. Have you heard anything like a shift in how your customers are talking. I know you guys are isolated from some of tariff stuff, just given your domicile. But with -- given some of the commentary from some of the European players, are you hearing -- has the conversation shifted a little bit towards more cautious production with some of the WLTP and some of the potential for the U.S. tariffs? How have those discussions kind of progressed? And how do you feel your customers are thinking right now?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Yes, the WLTP is a pretty identifiable issue. From a longer-term perspective, that actually reinforces what's happening in Europe around the need to comply to real driving emission. And that's a positive for Sensata in terms of our secular growth. When we look at the impacts inside of the quarter, that's a test regimen that is in some cases slowing vehicle cycle to market. So seeing a little bit of demand movement from third quarter to fourth quarter in terms of its impact on us, but it's not a highly material development for Sensata.

Operator

The next question comes from Steven Fox of Cross Research.

Steven Bryant Fox - *Cross Research LLC - MD*

Martha, during your prepared remarks, I think you implied that you're seeing a pickup in cross-selling between controls and sensors with CST integrated. Can you just sort of give us some color around how that's actually occurring, what kind of products, market, et cetera?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Yes, I mean, this is part of the strategy that we put in place. So it's letting us do things like increase our distribution channel, which is quite small and bring more to those -- that channel to market. In other cases, when we look at things like variable control that's happening inside industrial motors and in things like HVAC, we are on both sides of that. So we're now able to bring sensors that go into the input for the overall control of the system. And we're sitting in the protection application for the motor itself, just to give you some specifics of how that works. So those are one example, there are many more.

Steven Bryant Fox - *Cross Research LLC - MD*

No, that's -- I appreciate the color. And then just to be clear, Paul, when I think about the operating leverage you produced in the quarter, I guess 100 basis points of organic margin expansion. If you broke that down between volumes versus productivity, et cetera, lower acquisition costs, spending, et cetera, can you just sort of give us a sense for how that breaks -- the 100 basis points break out?

Paul S. Vasington - *Sensata Technologies Holding PLC - CFO, CAO & Executive VP*

Sure. I would characterize it as continued improvement on our cost reduction initiatives, particularly in our manufacturing areas. We've also seen, as the strategy has played out, the expansion of businesses beyond the automotive business. And that is driving a favorable mix in terms of the business. And then it's the continued cost control around our SG&A, which would be the third component of that.

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Steven Bryant Fox - *Cross Research LLC - MD*

And so those items obviously account for a majority of it as opposed to just natural leverage from higher volumes. Is that a fair assumption?

Paul S. Vasington - *Sensata Technologies Holding PLC - CFO, CAO & Executive VP*

We actually do get some leverage on the natural volumes. But that's reflected in our gross margin expansion as well. So I'd say it's 1/3, 1/3, 1/3 for the 3 things I mentioned.

Operator

And next, we have a question from Brian Johnson of Barclays.

Brian Arthur Johnson - *Barclays Bank PLC, Research Division - MD & Senior Equity Analyst*

I have a couple of questions just really around the product mix directions. Within HVOR, you talked about the growth of multiple end markets. But could you give a sense of kind of where -- what kind of systems that content is going to? Is it -- how much is engines? And how much are things like you flagged, like brake, steering and other applications?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Tough to break that out. The system piece of that is growing much more quickly. So we're getting to the point where that's getting close to overall parity. Having said that, we're also working on electrification opportunities in HVOR, although I think those are a little farther out on the time horizon. And that has an impact on the powertrain side.

Brian Arthur Johnson - *Barclays Bank PLC, Research Division - MD & Senior Equity Analyst*

Okay. And second question, between Swindon and Schrader, you brought in wireless sensing capabilities. How much is that driving the content growth either in any of the 2 to 3 segments? And what's -- particularly, you must have been at Farnborough this summer. Are you getting some traction in aerospace around wireless sensing?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

So the wireless piece is really important in China for auto and HVOR, as we're early days on TPMS. And then with some longer-term growth initiatives, we're seeing some really exciting opportunity to bring a wireless hub to the commercial truck trailer market, engaged in doing that. And then finally, that same capability allows us to engage with customers on battery management systems for both auto and industrial customers. So we're heavily engaged on that as well. So it's an important skill set that came along with that acquisition. Less meaningful near term in aero, as you know, that's very long cycle, when we look at what those opportunities are. We do have engagements around tire pressure sensing in that space as well.

Operator

And the next question will come from Mark Delaney of Goldman Sachs.

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Mark Trevor Delaney - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

First question is on buybacks. And the company has been moving pretty quickly through its repurchase authorization. And Martha, I think you said in your prepared remarks, you would expect after completing this one to go to the board and look for more. Has there been any evolution about how the company is thinking about the cadence of buybacks? And is this something that would be sustained? And how are you thinking about balancing buybacks with M&A going forward?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Yes, we do think that buybacks will be an ongoing component of our overall capital deployment and a meaningful ongoing deployment. So by meaningful, certainly above -- 25% or above and on an ongoing basis. So we would expect that to range in terms of percentage of our free cash flow. We expect to be repurchasing stock as we move into 2019 as well. At the same time, what we do is very returns-based-oriented. So our M&A pipeline continues to be active. But it continues to be much more bite-sized in its orientation and focused outside of auto. So that being said, then we would expect to be doing both share buybacks and bite-sized M&A. And we've got the capacity then to make sure that repurchases are a meaningful part of our ongoing deployment.

Mark Trevor Delaney - *Goldman Sachs Group Inc., Research Division - Equity Analyst*

That's helpful. And then a follow-up was just a clarification on the new organic revenue guide for all of 2018. And for the up 5% to 7% organic calculation, can you just clarify how exactly the valves divestiture is being factored into that? Is it just stripped out of essentially 4Q in both this year and last year? Or is it stripped out of all of 2018 relative to an adjusted 2017?

Paul S. Vasington - *Sensata Technologies Holding PLC - CFO, CAO & Executive VP*

It's stripped out for the period that we don't expect to own it.

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

So it is not out of history. So our organic growth is offsetting the impact of divesting the valves.

Operator

The next question comes from Craig Hettenbach of Morgan Stanley.

Craig Matthew Hettenbach - *Morgan Stanley, Research Division - VP*

Question on the industrial business and looking like it's been the strongest growth in over a year. And I know you mentioned some CST portfolio improvements. Any commentary on just the cyclical backdrop and kind of how you're seeing from a visibility perspective as you go into the second half for industrial?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Yes. From an end market, it's quite diversified. And so we keep our eye on things like the PMI index around the world, which is performing well. But it's really important to emphasize that primarily what we're seeing here is secular growth. And so we see demand for more industrial sensors for all the reasons we've talked about that are driving overall Sensata's growth. So the need for more efficiency, more variable control, cleaner applications, we're seeing some electrification now impact opportunities in the industrial space. And that's primarily what's driving our business.

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Craig Matthew Hettenbach - *Morgan Stanley, Research Division - VP*

Got it. And on the point of electrification just for EVs, as you look at that kind of emerging, can you talk about just your design activity? And clearly, it's small today from a volume perspective but expected to ramp. But just what your visibility is into that over the next couple of years in terms of as you see that market ramping up to volume.

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Yes. So the design cycle, I would say, is similar to what we're used to seeing in the auto market. So the work that we're doing today is in the 3- to 4-year time horizon. But I really hope that you took the point that we've done work in the past in systems that are now being utilized on first-generation electric vehicles. And that's driving our growth. So the regenerative braking example is a good one. That's very low installation rates today. And we expect that to drive another $50 million in revenue in our overall braking sensor revenue. And that's designed in. So it really is a range of opportunities, some of which we're enjoying right now and will ramp as EVs ramp and added content that we're focused on to bring new sensors to these challenges. And that's more in the 3- to 4-year time horizon.

Operator

(Operator Instructions) And our next question comes from Matt Sheerin of Stifel.

Matthew John Sheerin - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Senior Equity Research Analyst*

Just regarding your commentary on China auto demand, which continues to be robust, how much of that is coming from the TPMS upgrade cycle versus other electronic content issues? And as you look to next year, looking against tough comps, do you continue to see that organic growth continue to be strong?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

TPMS is only one component of our growth in China. So the other elements that we've talked about, for example, the drive for clean and efficient, we're seeing a lot of content go into vehicles that will allow them to meet national VI standards in China, for example, so better efficiency and cleaner output. We're seeing the need for more convenience features. So automatic climate control is still not a highly installed application in China. And that drives our business as well. So it's quite broad-based. We do expect to see continued growth as we move into 2019 and expect that China will continue to lead our overall growth in auto.

Matthew John Sheerin - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Senior Equity Research Analyst*

Okay. And just a quick one for Paul regarding the share count for the year relative to your buyback program. Is that factored into the EPS guide for the year? Or will that not be much of an impact until fiscal '19?

Paul S. Vasington - *Sensata Technologies Holding PLC - CFO, CAO & Executive VP*

The share repurchase is reflected in our EPS guide for the year. And we would expect to buy shares fairly ratably over the next 6 months or so, subject to market conditions.

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Operator

The next question will come from Jim Suva of Citi.

Jim Suva - *Citigroup Inc, Research Division - Director*

I just have one question. In the past, sometimes there's been inventory being very lean or excess inventory that has then come back to either help or hurt Sensata in its different markets, whether it be HVOR or auto or even HVAC or different climate control systems. Can you just talk broadly about the channel inventory system of where you sit today and what you're hearing about channel inventory? Is it in balance? Are there areas of leanness? Are there areas of buffer and how we should think about that?

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

We particularly keep our eye on that, Jim, in China, where we've seen in the past less discipline, as you point out. And when we look at those inventories today, we are feeling pretty good, so really in line with normalized rates for that overall supply chain.

Jim Suva - *Citigroup Inc, Research Division - Director*

Okay. And is that regarding both -- basically all your end products or end markets about the different segments, so...

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

Yes, that's right.

Operator

And our next question comes from William Stein of SunTrust.

William Stein - *SunTrust Robinson Humphrey, Inc., Research Division - MD*

Just two, and I'll front-load them. First, hoping to get any update on the Quanergy investment and whether you're seeing any traction in improved cost-downs that would enable production runs there. And also if you could remind us of the benefits you're getting from prior M&A that are still flowing through the model and when you expect those to be fully realized.

Martha N. Sullivan - *Sensata Technologies Holding PLC - CEO, President & Executive Director*

I think relative to Quanergy, we've talked in the past about this being a longer-term opportunity for Sensata and that really being framed by the fact that there's a lot that has to happen beyond just LiDAR to get to Level 4, Level 5 autonomy. And so we keep our eye on that. And meanwhile, the developments are progressing well. It's really a combination of performance and then performance at cost. But I would emphasize the performance piece, it's a challenging sensor to put in place for overall mass production. But we're pleased with the overall development that we see. I'll let Paul speak to where we sit on overall synergies with acquisitions, most of that, I think, focused on costs. But recognizing we're seeing really nice revenue that really is coming out -- coming from the combination of our acquired businesses and core Sensata.

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Paul S. Vasington - *Sensata Technologies Holding PLC - CFO, CAO & Executive VP*

So Will, the expectation for cost synergies in 2018 was about $12 million. And we are tracking to deliver that. You'll see -- a large percentage of that will happen in the second half as we cleared through a lot of the buffer stock that we build. And now we're seeing the benefits of the lower-cost production in the new site. And so -- and I would refer you back to our Investor Day materials because we are tracking to those commitments that we shared at that time.

Operator

And that's all the time we have for questions today. I would like to turn the conference back over to Joshua Young for any closing remarks.

Joshua S. Young - *Sensata Technologies Holding PLC - VP of IR*

Thank you very much, Laura. I'd like to thank everybody for joining us this morning. We appreciate your continued interest in Sensata. And we look forward to speaking to you again in the near future. Thank you, and good day.

Operator

The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.

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