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EDITED TRANSCRIPT

ST.N - Sensata Technologies Holding PLC at Jefferies Industrials Conference (Virtual)

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PRESENTATION

David Lee Kelley - *Jefferies LLC, Research Division - Equity Analyst*

And welcome to the 2020 Jefferies Virtual Industrials Conference. My name is David Kelley, auto-tech supplier analyst at Jefferies and I'm pleased this morning to host Sensata, a global leader in sensors and sensor technologies across a number of end markets. And joining me as Sensata's CEO and President, Jeff Cote; Executive Vice President and CFO, Paul Vasington, and VP of IR, Jacob Sayer. (Operator Instructions)

So Jeff, Paul, if you would like to kick it off, I believe you have a quick presentation and then we can jump into Q&A.

Jeffrey J. Cote - *Sensata Technologies Holding plc - President, CEO & Director*

We do. Thank you very much, David, for hosting us and for everybody for joining. I'll spend a few minutes going through some slides, and then Paul and I will take your questions.

And if you refer to the slides on the screen here, some of you may know Sensata, but we're a 100-year-old industrial technology company. And although you may not -- some of you may not recognize our name, I can guarantee that you use our products every day in your homes, in your cars, in your places of work and in the transportation modes that you choose.

In 2019, we had about $3.5 billion of revenue. We employ about 21,000 people globally, and we operate in 12 -- 11, 12 countries. So we're very global. We have a strong legacy of designing and manufacturing, hard-to-do mission-critical sensors and electrical protection. And at the core, we help our customers solve their most difficult challenges in terms of meeting regulatory requirements or other initiatives that our customers have. And more and more, these customers are asking us to extend beyond just component level into subsystems, software and other devices that deliver valuable insight to them and control their systems.

We focus on high-value, high-growth segments, and we have a proven variable cost model and the most recent quarter of that we went through and managing through these challenging times is a demonstration of that. We also have a long history of continuous improvement that allows us to generate a differentiated margin in our business, in the core business. And also allows us to extract significant value and synergy associated with the businesses that we acquire.

We're not capital-intensive. We spend about 4% of net revenue on capital every year, and that allows us to convert a lot of our earnings into cash. And it also provides significant flexibility regarding capital deployment in a value-creating way toward M&A and share buyback. We serve a variety of OEMs tiers and more and more aftermarket customers as well across a number of end markets, including automotive, heavy vehicle and off-road, including agriculture and construction, also recreational vehicles, aerospace, both defense and commercial and a variety of industrial end markets, including smart buildings, factories, smart factories, clean energy and a number of other diversified industrial segments.

The slide that Jacob has up here illustrates that it's not one application that we serve. This is a demonstration of the number of applications that we might serve in some of these end markets that I just quoted. So there's no significant revenue concentration in any one of the applications. And as you can see, there are dozens, if not hundreds or thousands of different applications that we would be serving in those end markets.

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On Page 5, we benefit from a number of trends that are impacting the end markets we serve, including the need for clean and efficient systems as well as trends associated with Electrification, Smart & Connected or Internet of Things and also autonomy trends that are impacting those markets. And that allows us to bring products and solutions to market and generate long-term secular growth, which, again, is being demonstrated in these periods of time when the market is declining.

We are outgrowing the market even in a declining market. And we've demonstrated that secular growth over a number of years and given the long nature cycle of our business, meaning that the business we sell today will generate revenue 2, 3 years in the future, we have a lot of visibility into that secular growth, and we have a lot of confidence in that. Over the last 3 years, we've sold over $400 million of new business. And in 2020, despite everything that's going on in the market, we're in a trend that's faster than that, which continues and builds our confidence regarding long-term secular growth in the business.

On Page 6, we talk a little bit about our mega trends. We continue to believe that these megatrends and the investments that we're making in them across Electrification, Smart & Connected and autonomy, drive not only our -- will not only drive our market -- end market diversification, it will increase our long-term growth rate. And it will provide very important competitive advantages for us as these trends truly transform the end markets in the customers' businesses that we serve. And despite the impact of COVID-19, we do not see any evidence that our customers are slowing the investments in these megatrend areas, and we're continuing to invest alongside them. In our most recent earnings call, we talked about pulling that investment dollar amount out. So we provided more transparency into the investments we're making in this area. And it's our intention to continue to make that investment even in challenging times.

On the Electrification front, we're expanding the solutions that we provide across critical applications, across all of our end markets. So it's not just an automotive electrification theme, but across all of those end markets that we serve. And those trends are prevalent in each of those end markets.

And in the second quarter, we closed another $50 million of new business associated with Electrification, year-to-date, over $100 million. So good progress on that in terms of the acceleration of these trends, which inevitably will happen as broad legislation, such as the European Green New Deal go around the world. That will continue to increase opportunities for us and represents over a $6 billion addressable market for Sensata by 2030. So a very large market segment that's opened up associated with the capabilities that we're building organically, and we're acquiring.

On the Smart & Connected front, we've talked about the proof of concepts that we have ongoing with many large fleet managers, and we're confident in our ability to convert these into orders by the end of the year. And as part of this initiative, we're also engaging with several telematics companies that will allow us to transmit data that is collected on equipment or on vehicles with using Sensata's vehicle area network to the cloud to provide valuable insight to fleet managers. And so we're seeing great progress there. And this initiative opens up over $1 billion market on the OEM front and over a $7 billion market for us on the fleet management front by 2030. So you can see that we're targeting not only difficult applications, but we're targeting segments and growthful areas that are very large in terms of their addressable market, which should provide lots of runway for our growth.

Page 7, just some key takeaways. I believe we're very well positioned to navigate both the near-term and the long term. And I think the near term, we've demonstrated that. And in the long term, if you follow us as a company, you know that we're steady through that period of time, and we're very confident in the long term. We have a strong balance sheet. We have strong cash flow. We have a lot of cash on the balance sheet. We have $1.2 billion more than that given the bond offering that we just went through, and I'm sure we'll go through some of that in our -- in some of our Q&A. Paul will touch on that. I think it's an excellent transaction demonstration and the confidence in the long-term of the company given where that was executed and where the rate was. And we have taken the actions to align our cost structure to the new market realities. So we'll see some good growth in earnings from here as well.

We see a lot of strong new business opportunities, as I mentioned, which gives us confidence in that outgrowth as we look forward, and we're investing in and we're acquiring innovative technologies and solutions, which will allow us to address very large markets as we go forward. I mentioned over $6 billion in Electrification, $8 billion in Smart & Connected, and more recently, an acquisition of our radar business, PRECO, which opens up about a $600 million addressable market and heavy vehicle off-road associated with autonomy. And then they're -- obviously, our core business focus is on over a $20 billion market segment associated with regulation associated with clean, efficient and safety regulations around the world.

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So that's the quick summary. Why don't I stop there, and then we can go to Q&A.

QUESTIONS AND ANSWERS

David Lee Kelley - *Jefferies LLC, Research Division - Equity Analyst*

Okay. Great. Jeff, really appreciate the rundown. And maybe I'll kick things off here and then happy to take audience Q&A at the end. And I just wanted to start with you since you're now 5 months into the CEO seat. And as we've discussed, you picked an exciting first 5 months to be on the job.

I guess, could you walk us through your perspective of Sensata, given your history at the company? What you've learned in the first 5 months? And I know it's early, but any changes in strategy or approach that we should expect?

Jeffrey J. Cote - *Sensata Technologies Holding plc - President, CEO & Director*

Yes. Sure. So I guess I'd start with -- thank you. Many of you have reached out to me. I've been with Sensata for 13 years. I started my career with Sensata as the Chief Financial Officer. So I've met with many of you, and many of you have reached out to express your -- in many instances, your support and also advice along the way, and I really do appreciate that.

And so I've done a number of roles within the company, starting as CFO, Chief Operating Officer, President. And so I've spent a lot of time in our plants around the world and also with our customers. I think that gives me a unique perspective associated with the operations of the business. And I continue to be incredibly impressed with our organization's ability to adjust. We're a very flexible, dynamic company. And we have demonstrated the ability to do the right things that we need to, to be able to emerge from periods of disruption stronger. And that's been quite impressive. Fortunately, we've only seen a couple of those disruptions during my tenure here. But in both instances, I see the teams globally pull together to make the tough decisions, to do the right things to emerge from this a stronger company on many fronts.

We have unique capabilities and solutions that set us apart from the competition. We have very long-standing customer relationships, decades of working with customers, again, helping them solve their most difficult challenges and making sure that we can deliver as they scale their businesses. And so I feel very good about our ability to navigate through things, difficult times and growthful times. I've seen both during my time here. And I feel very comfortable and confident in our management team's ability to be able to do that.

From a strategy standpoint, given that I have been here for over 13 years, safe to say, I've been involved in the development and the execution of the strategy over time. However, over the last 3 years, as we've been managing through our internal succession plan, I've been more intimately involved in that. And during that period of time, you've probably noticed a shift toward megatrends, toward more diversification of the company. That just means that we'll be more stable during volatile periods. It does not mean that we don't really like what -- being experts and strong -- having a strong presence in automotive because I think a lot of the capabilities we bring to the other markets and the margins we're able to achieve in those other markets as a result of our strong position in automotive and the volume and scale and so forth that automotive brings to us. But a desire for more diversification over time, a desire to focus on these megatrends in these very large market segments that we'll be forming, have been really part of our strategy over the last several years, and they will continue to be. So no major changes in terms of strategic development and execution. To me, it's all about execution of that strategy. I think we clearly have the right strategy and making sure we execute on that over time is the most important focus area for me and for the team.

David Lee Kelley - *Jefferies LLC, Research Division - Equity Analyst*

Okay, great. And you referenced your core automotive strength, and that's where I wanted to go next. The auto industry does appear to be one of the first to recover from the recent disruption. Although global production is poised for what's going to be a third consecutive year of contraction.

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So the bar is set fairly low coming out of the downturn. Can you talk about, a, what you're seeing in the channel; and b, what you're hearing from customers right now?

Jeffrey J. Cote - *Sensata Technologies Holding plc - President, CEO & Director*

Yes, absolutely. So it's been a very, very tough couple of quarters. First quarter, we saw significant drop out in March as our customers started to pull things in. We -- and we -- you might remember, we talked about the fact that we allowed those orders to drop out in the first quarter despite what we could have done, which is held them to their order rates. But we just knew by doing that, we were going to see an even tougher second quarter if we held them to that.

From first to second quarter transition in the automotive business, I think it's safe to say that it's the most challenging quarter that we've ever seen as a company. In terms of the sequential revenue, North America was down 70%, Europe's down 60% versus -- excuse me, quarter-over-quarter, second quarter or second quarter of the year. So dramatic shifts. Interestingly, China was up 4% because China saw the decline in the first quarter of the year.

Now the silver lining associated with a very difficult second quarter is a transition to better outcomes. And so still quarter-over-quarter third '19, third 2020, we'll see some declines in those end markets, but we're going to see a sequential improvement of about 30%, 35% Q2 to Q3. So significant growth from there. And based upon the order books that we see, we would expect an improvement into the fourth quarter as well. We didn't provide fourth quarter guidance. But if you look at sort of the third-party forecasters, you would expect that to continue to increase in the fourth quarter.

And so different from the '08, '09 time frame where it took 4 to 5 years for North American auto to get back to the 2007 levels, we're seeing a pretty dramatic snapback in most of the regions that we serve. Yet to sort of determine how that will actually play out, but certainly, if you look at the transition Q2 to Q3. And that's supported by the order book that we have. We've talked about the fact that -- on our call that we see a very strong order book. But we're being cautious because, candidly, that order book that we've seen from our customers over the last several quarters hasn't panned out to what it originally was. And so there's been more volatility in the order book. But we're seeing more stability, measured by customer orders to shipments and the ratio between those and we're seeing much more stability in the month of July than we saw during all of Q2 and in March as well. So more stability, more positive views from customers, which is giving us reason for optimism, but again, we tend to continue to be very cautious and make sure that we're just dealing with it as it comes to us.

David Lee Kelley - *Jefferies LLC, Research Division - Equity Analyst*

Okay. Great. And maybe the follow-up then for Paul. I was wondering if you could talk about inventory levels. What you're seeing heading into the back half? We've had a Q1 build in China, a steep Q2 industry decline. So maybe positioning of the inventory going into the back half of the year ahead of some magnitude of recovery.

Paul S. Vasington - *Sensata Technologies Holding plc - Executive VP & CFO*

Sure, David. I can address that. Jeff, if you want to add any color. As it relates to Sensata, we talked about an inventory build at our customers of about $25 million in the first quarter. And that helped our outgrowth to the end market, and we called it out. And we gave specific guidance or input around what that inventory build was for automotive, and it was about 300 basis -- maybe 310 basis points of outgrowth related to inventory.

We expect that inventory, which is inventory that our customers built to support their supply chain to work itself off throughout the year. And so by the time we get to the end of the year, the impact will be neutral to the year. We did not see much change on a net basis in Q2. So we saw some increases and decreases in inventory of customers. But for the most part, it was a net neutral for Sensata. And so we think there's a $20 million, $25 million of inventory that will work itself off in the second half. And that is contemplated in our guidance.

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As it relates to industry, I think inventory levels in North America, in China, in decent shape. Europe, much tougher to get visibility to inventory levels. Like I said, I think the second half, we'll see some impact of that inventory getting worked off. I don't know, Jeff, if you want to add anything.

Jeffrey J. Cote - *Sensata Technologies Holding plc - President, CEO & Director*

Yes. I think that's it, Paul. I mean, the only thing -- other thing I would point out is that others may be seeing more inventory than we are, primarily because we made a decision to allow our customers to drop out. And as painful as that was, we didn't want the inventory stuff -- or excuse me, the channel full of inventory so that we had a harder time understanding the raw demand. And so I think that's part of the reason why the inventory impact for us is pretty small and manageable.

David Lee Kelley - *Jefferies LLC, Research Division - Equity Analyst*

Okay. Great. And you touched on North America, Paul. And whether it's Paul or Jeff, whoever wants to answer. I think your outlook for North American auto production is a bit on the cautious end. Although we have heard similar cautious commentary from others and many have noted visibility, especially going into the fourth quarter is low. I guess, could you just talk about what you're seeing in North America specifically as it relates to order patterns and demand?

Jeffrey J. Cote - *Sensata Technologies Holding plc - President, CEO & Director*

Yes, sure. We are -- we do have a more conservative view in North America and Europe than IHS. We have a slightly better outlook in China. And this is not a new phenomenon, right? I mean, we always have a slightly different point of view than third-party forecasters, but the magnitude is significantly higher in the third quarter. So globally, we have about a 1.7 million vehicle variation from IHS in terms of our forecast, which translates to a very significant revenue number, as everybody is pointing out of $60 million of revenue.

And largely, it's based upon a couple of things. It's caution around potential resurgence and the impact that, that would have in terms of lockdowns. It's caution around supply chain stability associated with, not us, but someone else or something else causing a disruption in the automotive supply chain. And it's also some caution associated with the order patterns, as I mentioned a bit ago, which is if we -- the billing or the bookings rate that we see with our customers has not been as clear an indicator of the outcome over the last several quarters.

Now again, it's stabilizing considerably but that indicator has not proven out over the last couple of quarters of being the best. And we want to make sure that we're applying the appropriate level of caution around this to ensure that we deliver. And again, we've sized the business with an expectation around where we would expect normalized demand. And we want to make sure that we're sized right for ultimately where things land.

If things get better, and by the way, I hope IHS is right. We all hope IHS is right here, right? We hope that things continue to go in that direction. We will be prepared to deliver it. So it's not a question of the ability to deliver. We'll be able to do that. And we'll continue to provide insight into what we're seeing. But that's the primary reasons around the disconnect between us and the third-party forecasters.

David Lee Kelley - *Jefferies LLC, Research Division - Equity Analyst*

Okay. Great. That's helpful. And then I wanted to move to Sensing Solutions. You have various end market exposures there. Maybe if you could walk us through puts and takes of what you're seeing across markets like aerospace, industrials and appliances. And then specific, too, in the industrial business, how are lead times currently? What do you see as far as the channel build going into the back half of the year?

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Jeffrey J. Cote - *Sensata Technologies Holding plc - President, CEO & Director*

Yes. So our industrial business down, call it, 15% in the second quarter versus the second quarter of 2019. So it's significantly less than some of the other end markets that we serve. I think that's pretty consistent with what others are seeing across industrial markets. It's weird to say 15% is a lot better, but 15% down is a lot better versus the other markets.

Third quarter, we're expecting, call it, 13% to 15% off the third quarter of last year, up sequentially a little bit. But again, it's not snapping back as strongly as some of the other markets that we saw a significant decline in. On the aerospace side, market down about 32% in the second quarter. We saw a little bit more of an impact in the second quarter, primarily due to our aftermarket business. So we saw a contraction in inventories on the aftermarket given the significant decline in flights. In third quarter, similarly, we're expecting a 25% to 28% down, but up sequentially in second quarter or third quarter. So we do see some recovery there. On the industrial side, there have been some really positive things and not only for the business, but us feeling good about our contribution to the community. We did put in action very quick accelerated programs to provide pressure sensors for medical devices associated with ventilators, which was a really great program for us to work on. Our medical business is not a big part of our industrial business. But it was about a $10 million bump for us in the second quarter, which was again, great for the business, but also really good to feel as though we're contributing to the broader cause.

And longer term, we're investing in areas on industrial, like smart manufacturing building, clean energy, which are really strong growth areas for us. And so we see lots of opportunity there that we're continuing to work on, on the industrial side.

In terms of lead times, we're not seeing any major change in lead times from our customers. But we do know that some of our customers, specifically on the industrial side, if any of you have recently been able to try to purchase a major home appliance or air conditioning system, there are some shortages in the overall markets in terms of the supply chain challenges associated with that, but I feel confident in that market's ability to snap back. We've, as I'd mentioned, being able to deliver for all of our customers, but it's a complicated supply chain, obviously. And I think you're seeing a little bit more disruption associated with some of those end markets in industrial than you have seen in some others.

David Lee Kelley - *Jefferies LLC, Research Division - Equity Analyst*

Thanks, Jeff. And we've got about 5 minutes left. I do have a few audience questions I want to get to in the chat here. So first one, you've identified secular trends that I think other market participants agree with. Can you talk about the sources of the competitive mode that gives Sensata an advantage over some of these other competitors, whether it's scale to deliver products at lower cost? Or how else you see your competitive advantage playing out? And then how should we think about market share in areas like electrification and connectivity go forward?

Jeffrey J. Cote - *Sensata Technologies Holding plc - President, CEO & Director*

Yes. So in terms of competitive advantage, let's just make sure we focus on the applications that are the hardest to do, that are truly mission-critical, right? And so these enable our customer systems to operate. And if they don't work, bad things happen, right? So you pick any 1 of our applications, a pressure sensor and a braking system, a high-voltage contactor in an energy storage system. If that component does not work in the application, you can imagine really bad things happen. If you're braking system in your vehicle fails or if the circuit protection in an energy storage system doesn't work.

So that we pick the mission-critical ones. What that does is it makes -- it creates an environment where there are only a few players that can compete there. And if you look across all of the end markets we serve, all the sockets that we serve, it tends to be 4 or 5 major competitors. It's not dozens, right? So that creates a bit of a competitive mode. So there's an opportunity for all of them to see strong growth. And those competitors vary by application, by end market. But that's a common theme. When you get into these mission-critical applications, there are only a few companies that our customers are comfortable going to for these mission-critical applications. The second one was exactly what you pointed out. Right, and it's what I referred to earlier. Because we serve a variety of end markets and some end markets which have very significant volume. And because we approach our solutions from a building block standpoint. Everything is -- when we go to build a new application or develop a new application for our customers, not a clean sheet. We start with building blocks of technology that are used in other end markets where we have high volume, both from a manufacturing standpoint, but also from a supply chain standpoint. And so the use of those building block approaches to the development

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of solutions, allows us to be able to get to market faster, but also be able to scale faster and be at a cost point that we can be highly competitive and still generate a great margin for our investors.

David Lee Kelley - *Jefferies LLC, Research Division - Equity Analyst*

Okay. And then one more from the audience with a couple of minutes left here. This one's on M&A. How robust is the pipeline? Are there more deals like PRECO in the works? The size of the opportunities? And if we look out over the next 6 to 9 months, how much would you estimate you might spend on M&A go forward?

Jeffrey J. Cote - *Sensata Technologies Holding plc - President, CEO & Director*

Sure. Paul, do you want to get that one?

Paul S. Vasington - *Sensata Technologies Holding plc - Executive VP & CFO*

Sure. I was on mute. So we have a very robust pipeline of opportunity that we're pursuing. But we're taking a very balanced approach given the environment that we're operating in right now. PRECO was a company that we were engaged with for quite a while. As Jeff said, it's an important first step for us into autonomy and ADAS, and we're very excited about it as a platform for growth in there, and it really supports our heavy vehicle and off-road business in terms of its offering to its customers. The pipeline as we've said in the past, right-sized bolt-on acquisition type properties where they advance our initiatives and efforts into the megatrends. It helps diversify our business. And so we're going to continue to look at opportunities. We need to be mindful of maintaining strong financial flexibility in the current market, current economic environment. But we want to continue to be relevant and growing organically to the extent that they are value creating, aligned with our strategy and in line with how we want to deploy capital in the current environment that we're dealing with.

David Lee Kelley - *Jefferies LLC, Research Division - Equity Analyst*

All right. Perfect. Thank you. I believe we are out of time. So Jeff, Paul, Jacob, really appreciate you joining me this morning, and thanks to everyone else for dialing in. Enjoy the rest of the day.

Jeffrey J. Cote - *Sensata Technologies Holding plc - President, CEO & Director*

Great. Thank you.

Jacob A. Sayer - *Sensata Technologies Holding plc - VP of Finance & CFO of Performance Sensing Gbu*

Thank you, David.

Paul S. Vasington - *Sensata Technologies Holding plc - Executive VP & CFO*

Great. Thanks very much. Have a great day.

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