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PRESENTATION

Operator

Good day, and welcome to Sensata Technologies Second Quarter 2021 Earnings Conference Call. (Operator Instructions) Please note this event is being recorded.

I would now like to turn the conference over to Mr. Jacob Sayer, Vice President of Finance. Please go ahead, sir.

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

Thank you, Keith. Good morning, everyone. I'd like to welcome you to Sensata's Second Quarter 2021 Earnings Conference Call. Joining me on today's call are Jeff Cote, Sensata's CEO and President; and Paul Vasington, Sensata's Chief Financial Officer.

In addition to the financial results press release we issued earlier today, we will be referencing a slide presentation during today's call. The PDF of this presentation can be downloaded from Sensata's Investor Relations website. This conference call is being recorded, and we'll post a replay webcast on our Investor Relations website shortly after the conclusion of today's call.

As we begin, I'd like to reference Sensata's safe harbor statement on Slide 2. During this conference call, we will make forward-looking statements regarding future events or the financial performance of the company that involves 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 GAAP -- Sensata's GAAP results for the second quarter of 2021. We encourage you to review our GAAP financial statements in addition to today's presentation. Most of the subsequent information that we will discuss during today's call will relate to non-GAAP financial measures. Reconciliations of our GAAP to non-GAAP financial measures are included in the earnings release and in our presentation materials. The company provides details of its segment operating income on Slides 11 and 12 of the presentation, which are the primary measures management uses to evaluate the performance of the business.

Jeff will begin today with highlights of our business during the second quarter of 2021. He will then provide an update on our recent progress in our key Sensata's Insights and Electrification strategic growth areas. Paul will cover our detailed financials for the second quarter of 2021, including organic and market outgrowth by business unit, our segment reporting and provide financial guidance for the third quarter and updated financial guidance for the full year 2021. We will then take your questions after our prepared remarks.

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

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

Thank you, Jacob, and welcome, everyone. I'd like to start with some summary comments on our strong performance during the second quarter of 2021, as outlined on Slide 4.

The business recovery we have experienced beginning in midyear 2020 continued during the second quarter. We responded effectively to increased customer demand, which drove 72% revenue growth from the prior year to a record $993 million, slightly above the guidance range we provided in April.

While automotive and heavy vehicle production for the period came in lower than expectations because of the semiconductor chip shortage, the industrial business was somewhat stronger. In addition, we benefited from -- during the second quarter from OEM efforts to replenish channel inventories.

We delivered $209 million in adjusted operating income during the quarter, representing 21.1% operating margin, higher sequentially as well as substantially higher than prior year period. This underscores our leading industry positions, our success in pursuing strategic growth factors and the strength and flexibility of our manufacturing and commercial model. I'd like to recognize the innovation and hard work of the entire team in achieving these strong results during the second quarter.

Looking at our performance year-over-year, we once again delivered strong market outgrowth, well above our target ranges. For the second quarter of 2021, we produced 2,850 basis points of outgrowth in our heavy vehicle off-road business and 990 basis points of outgrowth in our automotive business, excluding estimated inventory growth.

Since the beginning of 2018, we have produced 950 basis points of outgrowth on average in our heavy vehicle off-road business and 615 basis points of outgrowth on average in our automotive business. Paul will discuss our revenue outgrowth in more detail.

Sensata today is in a substantially stronger financial position, in part because of our excellent performance over the past year. For example, we generated $127 million in free cash flow in the second quarter. Our current cash balance of $1.9 billion positions Sensata well to continue to acquire businesses that will expand our presence in the critical growth vectors of Insights and Electrification, where we have already shown important initial success.

Based on our business wins in the first half of this year and the robust forward pipeline, we are confident that our new business wins in 2021 will exceed last year's strong level of $465 million. These new business wins demonstrates customer confidence in Sensata and fuel our ability to deliver strong outgrowth in the coming years.

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We continue to invest in our growth initiatives in areas driven by underlying megatrends and increased our organic investment to $14 million in the second quarter from $7 million in the second quarter of last year. These investments allow us to pursue significant opportunities and expand our product portfolio in high-growth areas.

On Slide 5, I share an update on our meaningful progress in Sensata Insights. I'll remind you that we provided a teach-in on our strategy and positioning in this area in early June. A replay of that presentation remains on our website. The Insights initiative addresses a market that is large and fast-growing and we are pleased by the traction we are gaining already with both current and new customers across various sectors.

Our revenue is on pace to achieve $100 million annualized in 2021 and grow in excess of 20% per year over the next several years. We have a substantial pipeline of over $800 million of business opportunities that have been identified. And we are working diligently to close these opportunities to fuel growth.

Our efforts in this area enabled us to close $20 million of recent new business awards. At this point, we have a very strong backlog of committed orders, representing 100% of the revenue we expect to generate from Insights for the balance of 2021. These accomplishments demonstrate the value we generate for our customers.

Included in those new business wins is a large win with a global transportation services business to track their refrigerated containers. This win alone is worth over $10 million in revenue per year on average as it rolls out. In addition, we were awarded a $6 million order from a large insurance carrier to drive growth of their usage-based insurance offering. This important win represents an instance where we displaced an incumbent supplier.

In yet another example, Sensata Insights recently won wireless gateway and wheel-end sensor business from a leading North American heavy-duty trailer suspension manufacturer to enable tire inflation and monitoring in a contract worth over $9 million in annual revenue once that program launches. These wins will fan out over time, generating recurring revenue for our business as our customers adopt our solution set.

Moving to Slide 6. Sensata is making excellent progress in winning new business in Electrification, in part because we take a holistic view of electrification and its growing impact on all the segments we serve. While electric light vehicles capture a lot of attention, to us, electrification also includes electrified heavy vehicles and the charging infrastructure necessary to support this ecosystem.

Sensata is already a leading provider of high-voltage protection on EVs and charging infrastructure. As the underlying industries that enable electrification become more widespread, we intend to be a key participant, supporting our growing base of customers.

Across our businesses, we have developed a substantial pipeline of over $600 million in electrification new business opportunities that our sales and engineering teams are cultivating. In the past 2 years, that pipeline has generated over $280 million in design wins that are in the development phase and in the coming years are expected to be incremental to our more than $200 million in estimated revenue from Electrification solutions in 2021.

We continue to win new Electrification business at an accelerated pace. During the quarter, a large, premier European heavy vehicle OEM awarded Sensata the design for a power distribution unit to help power their future electric commercial vehicles. Power distribution units combine contactors, fuses and battery management systems, all provided by Sensata. This strategically important business win is worth over $11 million in annualized revenue once it launches.

Our joint venture with Churod Electronics announced last quarter extends our electrical protection capabilities to mass market vehicles and other electrified equipment requiring medium-voltage electrical protection. This JV is already being awarded new design wins, including the battery protection contactor business of a large European OEM intending to produce EVs for the China market worth over $6 million in annual revenue.

In addition, at the higher voltage end, we recently were awarded a contactor design from a North American OEM, using these contactors for their electrified pickup trucks worth more than $18 million in annual revenue. This utilizes the GIGAVAC robust solution. Later in the year, we will webcast

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a teach-in covering our electrification initiatives so that listeners can gain a better understanding of our offerings in this space, the evolving market and our go-to-market strategies in this key growth vector for Sensata.

In sum, I'm pleased with our progress against these initiatives which supports our increased investment to pursue these large, fast-growing markets driven by secular trends. As I've said before, we see numerous opportunities to utilize our strong financial position, our engineering capabilities, supply chain and customer relationships to meaningfully enlarge our addressable markets through organic efforts as well as bolt-on acquisitions and partnerships within these megatrends.

I'd now like to turn the call over to Paul.

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

Thank you, Jeff. Key highlights for the second quarter, as shown on Slide 8, include record revenue of $992.7 million, an increase of 72.2% for the second quarter of 2020. Organic revenue increased 62.9%. The acquisition of Xirgo increased revenue by 4.4%. And changes in foreign currency increased revenue by 4.9%.

Adjusted operating income was $209.3 million, an increase of 179% compared to the second quarter of 2020, primarily due to higher revenues, partially offset by elevated costs related to the industry-wide semiconductor chip shortage, higher spend to support megatrend growth initiatives and higher incentive compensation aligned to improve financial performance.

Second quarter of 2020, the prior year comparison quarter, included $21.6 million in savings related to temporary furloughs and salary reductions in response to the negative impact of COVID-19 on our markets and business. Adjusted net income was $151.4 million, an increase of 447% compared to the second quarter of 2020, largely due to the significant increase in operating income. Adjusted EPS was $0.95 in the second quarter, an increase of 428% compared to the prior year quarter.

Now I will discuss our performance by end market in the second quarter of 2021, as outlined on Slide 9. Our organic revenue increase of 62.9% year-on-year is comprised of overall end market growth of approximately 45.4%, estimated customer inventory restocking of 6.1% and market outgrowth of 1,140 basis points for Sensata.

Our heavy vehicle off-road business posted an organic revenue increase of 95.7%, representing end market growth of 57.6%, estimated growth of 9.6% due to customer inventory restocking and 2,850 basis points of market outgrowth.

Our China on-road truck business continued to post better-than-expected growth from the accelerated adoption of NS VI emissions regulations. And we are benefiting from both a wave of electromechanical operating controls being installed in new off-road equipment and early stages of radar installations on heavy vehicles as a safety feature. We do expect market outgrowth to remain high for the balance of the year for our heavy vehicle business as the NS VI regulations in China have led to substantially increased content per truck.

Our automotive business posted an organic revenue increase of 74.9%, representing end market growth of 56.1%, estimated growth of 8.9% due to customer inventory restocking and 990 basis points of market outgrowth. Our automotive business benefited from new product launches in powertrain and emissions, safety, in electrification-related applications and systems. Vehicle inventories, especially in North America, remain in historic lows, signaling a tailwind to automotive market growth for the foreseeable future.

Our industrial business increased 29.2% organically as global industrial end markets continued to recover in the quarter. Strong growth in heating, ventilation and air conditioning, new electrification launches and supply chain restocking benefited our industrial business.

Our aerospace business increased 20.6% organically, reflecting somewhat improved OEM production in air traffic, which drives our aerospace aftermarket business. New product launches, primarily in defense, and improvements in aftermarket, enabled our aerospace business to grow faster than market this quarter.

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One of the reasons our outgrowth to market is so high this quarter is that the comparison revenue in the second quarter of 2020 was unusually low, reflecting widespread plant closures in response to COVID-19 outbreak. Slide 10 deconstruct this dynamic for you, showing what would happen if we compare this quarter's outgrowth to our normalized quarterly revenue figure instead of the low point in 2020. The resulting adjusted outgrowth of 1,640 basis points for heavy vehicle off-road and 640 basis points for automotive are still well above our target ranges, and these numbers are more appropriate figures to compare to other quarters on a stand-alone basis.

Now I'd like to comment on the performance of our 2 business segments in the second quarter of 2021, starting with Performance Sensing on Slide 11. Our Performance Sensing business reported record revenues of $741.9 million, an increase of 92.6% compared to the same quarter last year. Excluding the positive impact from foreign currency of 5.8% and the positive impact on the Xirgo acquisition of 6.6%, Performance Sensing delivered 80.2% organic revenue growth.

Performance Sensing operating income was $202.1 million, an increase of 232.6% as compared to the same quarter last year, with operating margins of 27.2%. The increase in segment operating income was primarily due to higher revenues, somewhat offset by elevated costs related to the industry-wide semiconductor chip shortage. The prior year quarter included savings related to temporary furloughs and salary reductions. Performance Sensing generated incremental margin of 43% in the second quarter and higher organic revenue as compared to the prior year period.

As shown on Slide 12, Sensing Solutions reported revenues of $250.8 million in the second quarter of 2021, an increase of 31.1% as compared to the same quarter last year. Excluding the positive impact from foreign currency of 3.1%, Sensing Solutions delivered 28% organic revenue growth.

Sensing Solutions operating income was $76.5 million, an increase of 37.1% in the same quarter last year, with operating margins of 30.5%. Like Performance Sensing, the increase in segment operating income was primarily due to higher revenues somewhat offset by elevated costs from the industry-wide semiconductor chip shortage. And again, the prior year quarter included savings related to temporary furloughs and salary reductions. Sensing Solutions generated incremental margin of 37% in the second quarter and higher organic revenue as compared to the prior year period.

On Slide 13, Corporate and other operating expenses not included in segment operating income were $74 million in the second quarter of 2021. Excluding charges added back to our non-GAAP results, corporate and other costs were $67.7 million, an increase of $27.8 million from the prior year quarter, primarily reflecting higher research and development and business development spend to support our megatrend growth initiatives and higher global incentive compensation costs aligned to our improving financial performance. The prior year quarter included temporary savings from furloughs and salary reductions.

We currently expect approximately $50 million to $55 million in megatrend-related spend in 2021, up 70% in 2020, to design and develop differentiated, sensor-rich and connected data solutions for the fast-growing and transformational mega transactors of Electrification and Sensata Insights.

Slide 14 shows Sensata's second quarter 2021 non-GAAP results. Adjusted operating income increased 179.1% and compared to the same quarter last year, and adjusted operating margin increased 810 basis points to 21.1%. The increase in both adjusted gross margin and adjusted operating margin largely reflects the rapid increase in revenue from depressed levels experienced last year due to COVID-19 pandemic.

We acted early during the pandemic to reduce our cost structure while continuing to invest in megatrends that are shaping our end market that we believe will enable us to deliver long-term sustainable growth. We've included an adjusted operating income margin walk from the second quarter of 2020 to the second quarter of 2021 on the slide.

As shown on Slide 15, we generated $127 million of free cash flow during the second quarter, representing an 84% conversion rate of adjusted net income. For the full year, we expect free cash flow conversion to be approximately 85% of adjusted net income. For full year 2021, we expect capital expenditures to be in the range of $160 million to $170 million.

Sensata's net debt-to-EBITDA ratio was 2.7x at the end of June 2021. Through increasing earnings and free cash flow generation, we expect our net leverage ratio to be near the bottom of our target operating range of 2.5x to 3.5x by the end of this year, absent further acquisitions.

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We have provided financial guidance for the third quarter of 2021, as shown on Slide 16. We expect to generate revenues between $920 million and $950 million for the third quarter of 2021, representing a reported revenue increase between 17% and 21% compared to the third quarter of 2020. Excluding the impact of foreign currency in the Xirgo acquisition, we expect an organic revenue increase of 12% to 16% in the third quarter.

Our current fill rate is approximately 98% of the revenue guidance midpoint for the third quarter. Our current fill rate appears stronger as compared to previous quarters and some customers in the industrial, in China transportation industries have extended their order lead times to better ensure supply. We estimate this extended ordering raises our fill by approximately 6% as compared to other periods.

We expect to report adjusted operating income between $189 million and $199 million. At the midpoint, adjusted operating income margin is expected to be 20.7%, which includes 140 basis points of increased operating costs associated with the global semiconductor chip shortage, net of customer recovery actions.

On the bottom line, we expect to report adjusted net income between $130 million and $140 million and adjusted EPS between $0.82 and $0.88, which includes a $0.01 increase from foreign currency at the guidance midpoint. At the bottom of the slide, we have provided an adjusted operating income margin walk from the third quarter of 2020 to the third quarter of 2021.

We are tightening the range of financial guidance for the full year 2021 and raising the midpoint as shown on Slide 17. For the full year 2021, while a degree of market uncertainty remains, in particular from the impact of the semiconductor chip shortage, we are anticipating a continuation of the improved and more stable economic and business conditions. We are also anticipating a return of normal seasonality, which includes sequentially lower revenue in the third quarter as compared to the second quarter and roughly flat fourth quarter revenue as compared to the third quarter.

Accordingly, we now expect to generate revenues between $3.77 billion and $3.84 billion for the full year 2021, representing a reported revenue increase between 24% and 26% year-on-year. Excluding the impact of foreign currency and the Xirgo acquisition, we expect an organic revenue increase of 19% to 21% in 2021.

We expect to report adjusted operating income between $782 million and $818 million, which reflects expectations for higher costs from the global semiconductor chip shortage and other inflationary impacts, somewhat offset by recovery actions we are pursuing with our customers. At the midpoint, our expectation for adjusted operating income margin is 21%.

On the bottom line, we expect to report adjusted net income between $544 million and $576 million and adjusted EPS between $3.42 and $3.62, which includes a $0.05 benefit from foreign currency at the midpoint of guidance. At the bottom of the slide, we have provided an adjusted operating income margin walk from 2020 to '21 to show the moving pieces impacting margins.

On Slide 18, we provide our revised estimates for OEM production growth for 2021 as compared to the expectations we shared in late April. We currently expect automotive production to rebound this year from last year, but at a pace lower than expected in April given further production slowdowns caused by the global semiconductor chip shortage. We are diverging from IHS production estimates for the year with a forecast for auto production that is more conservative than IHS.

We currently expect global automotive production to grow 5% for the year as compared to IHS at 9% in their July update. In addition, we are expecting third quarter automotive production for our markets to be about flat with production reported in the second quarter of this year.

On the other hand, our heavy vehicle off-road and industrial end markets are now expected to grow faster in 2021 than we shared in April. And in line with its normal pattern, we expect our industrial business to be seasonally lower in the second half as compared to the first half of 2021. These assumptions underpin our current outlook for revenue and earnings this year.

In sum, Sensata delivered an excellent second quarter with record revenue despite broad supply chain disruptions. We expect this solid performance to continue throughout 2021 as demonstrated by the financial guidance we're providing today.

Now let me turn the call back over to Jeff for closing comments.

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

Thanks, Paul. Let me wrap up quickly with a few key messages as outlined on Slide 19.

Sensata has responded very well to the rapid improvements in many of our end markets, demonstrating the strength, flexibility and reliability of our business and organizational model. It's enabled us to capitalize on the recovery in the end market demand and deliver on customer orders. Our quick response to shifting demand positions us well as a trusted resource for our customers.

We are delivering consistently robust end market outgrowth. We remain confident in our ability to sustain this attractive end market outgrowth into the future based upon our strong levels of new business awards and our large and expanding pipeline of new opportunities. We continue to invest in our megatrend-driven growth initiatives that are opening large and rapidly growing opportunities for Sensata across all of our end markets. We are making excellent progress in Sensata Insights and Electrification, as evidenced by the results so far this year as well as our new business wins in both areas.

We continue to believe that the overall business environment provides interesting opportunities to further strengthen our portfolio through strategically important, value-creating acquisitions or joint ventures. In addition, we are pursuing new technology collaborations and partnerships with third parties to expand our capabilities and accelerate our megatrend growth. We expect to continue to deliver industry-leading margins for our shareholders while also increasing investments in our growth opportunities and our people.

And finally, I'm excited about Sensata's long-standing mission to help create a cleaner, safer and more connected world, not just for our customers' products, but also through our own operations. We believe we are meaningfully contributing to a better world.

We are incorporating ESG considerations into our strategy to bolster our long-term sustainability and success of the company for all of its stakeholders. We look forward to reporting more in the future on this topic.

Now I'd like to turn the call back to Jacob.

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

Thank you, Jeff. (Operator Instructions) Operator, please assemble the Q&A roster.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And the first question comes from Wamsi Mohan with Bank of America.

Wamsi Mohan - *BofA Securities, Research Division - Director*

Congrats on the solid results. I was wondering if you could delve a bit deeper into your inventory assessment that you have broken out, which is very helpful. Where do you think this incremental inventory is building? And do you think that, that gets absorbed in calendar 3Q? Or does the guide include some further buildup of inventory?

And just a follow-up on that. You noted the sort of more conservative auto outlook versus IHS. Is that just purely based on supply constraints? And does that set up for a better '22 given the fact that your auto production view has come down materially for the rest of '21?

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

Sure, Wamsi, and Jeff and I'll both take that. In terms of the inventory estimate, how we do that is we have some centers that we ship that have very high market share. And based on the number of units we ship versus the production, we triangulate on a certain amount of our parts that are going into customer inventory versus going in to produce those vehicles. So it is an estimate, we think it's a pretty good estimate. And that's automotive.

And in the heavy vehicle, we do know that some of our customers are having initial provisioning for their NS VI-compliant platforms and that inventory will stick and stay in their inventory level. So we have a pretty good feel for it. It's not a perfect answer, but it's a good estimate.

In terms of what we're seeing around the second half of this year, we do think some of this inventory will unwind. We bring it back to last year in the third quarter, fourth quarter of 2020, we did see -- we did believe inventory levels were depleting at our customers. Then they were building inventory, we think, in the first half. And then the second half of this year, we'll see some unwind. So it is having somewhat of an impact sequentially on our revenue in the automotive business.

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

And on the second part of your question, Wamsi, on the automotive outlook. I think you're right, that's the primary driver of our more conservative outlook, supply chain constraints. It's been well publicized. There are some significant challenges associated with it. You see it as consumers, in terms of lead times for vehicles, number of inventory days in North America at an all-time low. So having lived through that over the last year, experienced the challenges associated with it, we're taking a more conservative view for the balance of the year.

And your added comment regarding the outlook for next year, I think, is absolutely right. Even with a recovery of 5% of -- in auto globally year-over-year, we see this substantially below where the peak markets for auto have been historically. So there's still a lot of tailwind for automotive growth of the markets that we're seeing in 2021.

Operator

And the next question comes from Samik Chatterjee with JPMorgan.

Samik Chatterjee - *JPMorgan Chase & Co, Research Division - Analyst*

Jeff, I just wanted to ask you kind of more on the acquisition comment that you had. And I think it sounds like given where the leverage is and given the kind of the success you're having, you sounded a lot more aggressive about [full-swing] acquisitions. Can you give us some color about like the pipeline of opportunities you're looking at. What areas are you more focused on? And besides kind of Insights and Electrification, are you looking at any other kind of pillars of growth that you want to kind of also invest in?

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

Yes. Great. So I'm not sure it's a more aggressive stance on M&A. We have a strong pipeline. We've had some good execution on M&A and joint venture-related activity already this year with Lithium Balance, Xirgo, the Churod joint venture. So we feel that we've got some really good momentum. We will stay very disciplined. The focus areas are around megatrends. So that's the exclusive focus of our M&A-related and joint venture-related activity. There'll be more bolt-on cereal. So the goal is to create more M&A growth every year rather than lumpy M&A growth.

And the criteria for M&A will be accretive revenue growth, differentiated margins. And again, we'll maintain our discipline in terms of evaluating opportunities and making sure we're highly confident we'll be able to generate returns for shareholders as well as expanding our presence in these markets that we're pursuing. Hopefully, that's helpful.

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Operator

And the next question comes from Luke Junk with Baird.

Luke L. Junk - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Jeff, just wondering if it would be possible to break out the $200 million in forecast 2021 Electrification revenue that you had in the deck by these 3 major end markets, so auto, industrial and heavy vehicle. And maybe also if you could speak to the relative growth rates you're seeing this year between those as well at least qualitatively.

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

Yes. So it's going to be more disproportionately weighted toward auto given that's where the business is focused in terms of the ratio of our overall company revenue. So I would say broadly, apply the same end market exposure. We're seeing very substantial growth there. We've -- we quoted that last year, we had about $120 million of Electrification business, so you can see it's substantial growth.

Now some of that is coming as a result of the shift from internal combustion engines to electrified, but we see a lot of content growth there. We've talked in many other occasions regarding the fact that the transition to electrified platforms is a tailwind for us in terms of content per vehicle and also content per piece of equipment. And the opportunities, we see them as being even more significant outside of light vehicle auto, right?

So when you talk about power distribution units for commercial vehicles, the amount of opportunity we have to serve broad infrastructure plays in terms of charging stations, we've talked about that. So we see this as being a pretty broad-based play in terms of growth opportunity for us as a company.

Operator

The next question comes from Joe Spak with RBC Capital Markets.

Joseph Robert Spak - *RBC Capital Markets, Research Division - Autos and Leisure Analyst*

Maybe just to get back to auto and the restock. I think last year you talked about maybe like $30 million to $35 million of restock and now it seems like another $35 million. So is the right way to think about that as the cumulative impact that -- of the inventory build? Or did some of that stuff from last year already -- already get unwound?

And then I guess related, like when we talk to the automakers, it doesn't really sounds to us like they're going to stop taking product because they want to make sure they can complete the vehicles when they receive missing modules. So I'm wondering if this is, again, your unwind is just conservatism, if you think this can actually play out differently and maybe that inventory build unwinds slowly or bleeds out over time?

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

And Joe, last year, if I'm correct, I think we talked about inventories being depleted in the third and fourth quarter and then a rebuild of those inventories in the first half of this year. And like I said, we use -- we triangulate on that impact based on sensors with a very high market share that we're shipping into the marketplace that are at higher shipment levels in production. So it seems as if our parts are ending up in warehouses to possibly be there when they're actually able to get that last module to make sure they can release it to cars.

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We've been seeing a much stronger growth trajectory because of this inventory growth and we do think if some of it unwinds, unwinds in the second half. But again, this is our best forecast and we'll have to see how it plays in the third quarter.

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

Joe, to add some color to what we're experiencing on this front, I think your observations are absolutely accurate, that our customers are going really deep on this. We're having multi-party conversations to make sure that we're being as coordinated as we possibly can regarding what we build to make sure that we can serve the customer. Because at the end of the day, it doesn't help if there are parts that are not in inventory and the vehicle can't be produced because of another supplier.

So there's a lot of coordinating activity that's occurring on that front to make sure that we can deliver what was a record revenue quarter. So a lot of work is being done to manage that process.

Operator

And the next question comes from Matt Sheerin with Stifel.

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

I wanted to ask about your commentary about the input costs, particularly semiconductor cost for you and your ability or inability to pass them along. Have conditions maintained the same or worsened? And do you have any visibility into when your own supply picks up? And then in terms of passing through those costs, how are those discussions with customers going?

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

The conversation with customers are going along as expected. It's a difficult conversation, but we're a strong partner and supplier to them. And so to the extent we can share those costs, they're willing to do that and we've had some success. So in the second half, the actual underlying gross costs are going up, but the recoveries are offsetting that. So good progress there, so that the net impact hasn't changed much from what we communicated back in April.

On the supplier side, Jeff, I would say, you want to add in here, we continue to -- and particularly, we're being very aggressive here in second quarter to secure inventory to make sure that we have our strong position in terms of ensuring supply. We've gone into the spot markets to buy material and feel like we're pretty well positioned from an inventory perspective to be able to serve the demand that we're seeing in the second half. Our inventory level is a little bit higher, but we're comfortable about it just given the disruption that is in the supply chain today.

Operator

And the next question comes from Amit Daryanani from Evercore ISI.

Amit Jawaharlaz Daryanani - *Evercore ISI Institutional Equities, Research Division - Senior MD & Fundamental Research Analyst*

I guess my questions will be around the calendar '21 guide. And if I think about the auto production estimate that you have, I think you're taking it down by 700 basis points versus what you had 90 days ago. So I guess the 2 parts will be, a, what is driving such a big reduction in your estimate for auto production numbers, and I think the lowest number from any auto ecosystem company?

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But secondly, you really haven't changed your overall top line assumption. So what is the offset to auto production coming down 700 basis points versus what you had 90 days ago? But the overall top line seems to hold up pretty well.

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

So we were trying to lay out for you that the auto production numbers that we see for Q3 is flat with Q2, because we don't see any real meaningful change in terms of the supply chain issues that the industry is dealing with. So it's flat Q2 to Q3. And then it improves in Q4, moves up, but not as much as what the third-party forecasts are projecting. And I think the evidence would suggest that the third-party forecast, while coming down, are not coming down fast enough to reflect what actually happens in the quarter.

So we think at some point, we'll get aligned there. But we think our estimate and our projection of the automotive production is a good one. It's an appropriate level given what we're seeing in the supply chain and what we're hearing from customers about their struggles in terms of ramping up capacity.

As it relates to what's offsetting, the heavy vehicle business continues to perform better as well as our industrial business. And so they are offsetting the decline that we're seeing -- actually more than offsetting the decline we're seeing, in the automotive.

Operator

The next question comes from Brian Johnson with Barclays.

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

Yes, just want to get a sense, and thank you for the update on Sensata Insights, both on this deck and the teach-in on how you're going after the $800 million pipeline, kind of the timetable for translating that into bookings. And then given, as you pointed out at the teach-in, this is a fragmented market around telematics, kind of what are you finding is the winning formula to secure bids versus ones that go to competitors?

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

Yes. So great question. So let me start with -- the pipeline is what would be referred to as contract value rather than typical sales or value. So that is a little bit of a departure from how we would, as a company, normally refer to the opportunity pipeline that we see. So -- and that's the way that sort of those types of more subscription-based or recurring revenue-based aftermarket models tend to refer to things.

It's more than telematics, right? So at the core of the offering is an ability to take information off a vehicle and get it to the cloud in the form of a telematics device. But what we're experiencing in terms of engagement with customers, as we combine these, what was the Xirgo and our internal Smart & Connected value proposition, is a much broader offering than just the telematics piece, right?

So Sensata, if you remember from the teach-in, Sensata brings the ability to get information off a piece of equipment through our very broad-based sensing capability. And then Xirgo brought the ability to accumulate that, get it to the cloud and analyze and provide data insights or information that would be more valuable. And so that's really the value proposition.

Clearly, they are leaders in terms of telematics, OBD port translation and so forth. But the real longer-term value creation is around that sticky information that's provided once the information gets to the cloud and they can do something with it. And that's what we're experiencing, more pull from customers as we have a broader solution set. And it's building really nicely.

The sort of thesis of the investment, combining it with the Sensata portfolio is working out quite nicely. More to come, early days still, but we're excited about the opportunity there.

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Operator

And the next question comes from David Kelley with Jefferies.

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

Just hoping you could give us a sense of how you're thinking about outgrowth going forward. And maybe specifically in autos, should we see a continued -- or do you expect to see a continued step-up in the second half outgrowth and specifically versus your longer-term targets of 400 to 600 basis points? And as we think about those outgrowth drivers, is there an opportunity that this kind of continued step-up in autos proves more structural?

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

Yes. So it's a great question. Let me start with we're really excited about the fact that we're exceeding the targets. But you might note that in our prepared comments, we spoke to the outgrowth over the last 3.5 years, which in auto was just slightly above the 600 basis points. In HVOR, it was considerably higher.

So let me speak specifically to what's driving that in HVOR. The auto one, we feel great about being at the high end of the range. We'll continue to evaluate opportunities to update guidance. But there's a lot of -- there are a lot of opportunities in the pipeline, those that we've won that give us confidence that we'll be -- we'll continue to be quite strong in auto.

The HVOR requires a little bit more digging into because the outgrowth is being driven by a pretty broad range of opportunities, but there are 2 that are quite large in terms of driving it above the average of 600 to 800, and that relates to the NS VI rollout in China, which has about another 6 months to a year where until it's fully rolled out.

So we would expect that to normalize a little bit. There are always other regulatory areas that will continue to drive, but NS VI was a big one driving that. So we're a little reluctant to change the 600 to 800 in HVOR.

And the second is the conversion from mechanical hydraulic to electro hydraulic controls. We had seen a pretty significant spike and pull associated with North America and Europe. And now we're seeing that in China as well. And so that's driving higher content than outgrowth values in the HVOR business.

So listen, at the end of the day, we're happy about being at or above the ranges. We'll continue to monitor it. And as we go forward and win new business, we'll give updates as to what we're thinking.

Operator

And the next question comes from Joe Giordano with Cowen.

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

Can you just talk about your relative positioning within EVs like on the different types of platforms, like higher-end models versus lower-end models with different power requirements and how your -- how Sensata's products are positioned in each of those?

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

Sure. So you'll recall that when we acquired GIGAVAC back in 2018, we did that because they had premier positions in the highest and most premier vehicles. And by the way, just to make sure everybody understands, when we talk about those higher-end vehicles, they are vehicles that have longer ranges and shorter charge times. It's not necessarily luxury vehicles. In the EV space, when we're talking about the technology that we need to bring to bear to help the customer solve the challenge, it's around charge time and range, which is what consumers are pulling.

At the time of that acquisition, we had a belief that, that was going to be the direction where the market was going. We think that's still going to be the case. But there will be a lot of the middle market, sort of EV market that was underserved without having more broad capabilities. So we added the Churod joint venture to the mix to allow us to be able to have a broader portfolio. So now I feel as though we're much better represented across all of those categories of electric vehicles.

And we're not done yet, right? So we continue to make organic investments and look for partnerships, JVs, acquisitions that will bring more capability to be able to serve these vehicle platforms as all of these customers adopt new models and they build out their next 5-, 10-, 15-year strategy in terms of product portfolio.

So really good success. We feel as though we're well covered now, not only across models, but geographically as well. And we'll keep working on it.

Operator

And our next question comes from William Stein with Truist Securities.

William Stein - *Truist Securities, Inc., Research Division - MD*

One of the things we've recently learned from some of the semi suppliers and our industry contacts is that we're hearing about auto OE customers decontenting in sort of opportunistic fashion in order to complete kits and get cars shipped to customers, essentially rolling back some innovation in order to complete the builds. I'm wondering if you're observing this trend, whether it's affecting your business and if you're contemplating this in the guidance.

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

Yes. So it's an interesting one. Obviously, OEMs are doing everything they possibly can to get more vehicles out. That is one of the tactics they're using.

So let me give you an example. If we had migrated to a next-generation sensor with that OEM due to cost reasons or whatever, tighter tolerances or faster response time, OEMs are willing to take a step back to go to the prior-generation sensor if the availability of the ASIC is there. It doesn't necessarily change the ability for them to meet the regulation, but there -- in some instances, there are cost implications associated with that. So as part of our product road mapping, we purposefully designed our new product to be able to give them a lower cost product going forward. And so sometimes we're taking a step back, we're having the commercial discussion regarding that.

But at the end of the day, the goal is to help our customers get more vehicles produced so that they can sell more vehicles. And so that's one technique that they're using, and they're looking at a lot of different ways to try to figure out how to get a complete set -- chipset to be able to make the cars.

Operator

And the next question comes from Nik Todorov with Longbow Research.

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Nikolay Todorov - *Longbow Research LLC - Analyst*

I understand that could be a hard-to-answer question, but what is your sense how much of your product could be sitting at partially built light vehicles or heavy vehicles right now? And how should that relate to the inventory destocking that you talked about?

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

I don't think we have visibility to where it is in their supply chain, but we estimated about $25 million of build this quarter. Things that we shipped that were in some -- it didn't go into a produced vehicle.

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

Yes. So that's all inclusive, right? It's hard for us to sort of really gauge where it sits. But when we do the math on our revenue growth and we back into the factors we know, including production numbers, we get about $25 million of inventory build in the quarter. Hopefully, that's helpful.

Operator

And the next question comes from Rod Lache with Wolfe Research.

Shreyas Patil - *Wolfe Research, LLC - Research Analyst*

This is Shreyas Patil on for Rod. Just a question, how should we think about bridging from the first half to the second half of this year? End market production should be higher in automotive and you are raising industrial and HVOR production and market expectations, but the guidance is implying about an 8% decline in revenue.

And then just quickly, if you could help frame the content benefit from the conversion to electronic hydraulics that you mentioned for HVOR.

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

Yes, on the revenue piece, it's -- like I said earlier, it's -- the reduction in automotive is being more than offset by improvements in both industrial and HVOR. I mean the improvement in HVOR and industrial are about the same in terms of the sequential step-up or at least relative to what we guided last time.

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

On the second part of your question, just to make sure I understand it, are you looking for a little bit more visibility into what this conversion from mechanical hydraulic to electronic hydraulic is? Is that the nature of your question?

Shreyas Patil - *Wolfe Research, LLC - Research Analyst*

It was one of the reasons you're achieving the above your prior target in terms of outgrowth. I just want to understand what -- the benefit that is to Sensata either on like a per vehicle basis or just some way to frame that.

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

Yes, got you. Okay. So let me -- so the application is an electronic joystick or integrated armrest in an agriculture piece of agricultural equipment or construction equipment or material handling equipment. So it's not a $5 content item.

Joysticks or integrated armrest can have ASPs anywhere from $50 up to $600, depending on the complexity of the design. So it's significant content. The volumes, obviously, are considerably lower than what we would see in a light vehicle market, but the ASPs are quite high and they drive significant content as that pans out. Hopefully, that's helpful.

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

Thank you, Rod (sic) [Shreyas]. And just to be crystal clear, I mean, in the second half versus the first half, we did talk about our industrial business coming back to its normal seasonal pattern, which is a weaker second half than the first half.

And in the heavy vehicle business, while it's experiencing great outgrowth in the fourth quarter typically is a little bit lighter seasonally. So that kind of accounts for the first half and second half and then also the automotive business declining a bit due to the low production levels.

Operator

And the next question comes from Michael Filatov with Berenberg Capital Markets.

Michael R. Filatov - *Joh. Berenberg, Gossler & Co. KG, Research Division - Analyst*

Just a quick question around aerospace. It looks like you're maintaining the market growth expectation for aerospace. But I think there are some indicators that suggest that the market backdrop is improving slightly. So just any commentary around aerospace market growth in the second half and if there's potential for upside, particularly because it's your highest-margin business.

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

Yes. It's a long-cycle business. It is largely -- demand is largely aligned to, as we said, OEM production and the air traffic. It is getting better. But this is a business that's pretty small relative to the rest of Sensata. So a few million of improved revenue, we'd expect to see in the second half versus the first half and it is very profitable. But it's not going to be a major needle mover this year, but it is showing signs of improvement, which is great news.

Operator

Thank you. And at this time, as there are no more questions, I would like to return the floor to Mr. Jacob Sayer for any closing comments.

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

Thank you, Keith. I'd like to thank everyone for joining us this morning. Sensata will be participating in upcoming virtual investor conferences this quarter, including Jefferies Technology Conference and the RBC Global Industrial Conference during the upcoming quarter. As Jeff mentioned, we're also planning a teach-in about our Electrification initiatives later in the year, and we'll share details of that event ahead of time.

We look forward to seeing you at one of those events or on our third quarter earnings call, which will happen in late October. Thank you for joining us this morning and for your interest in Sensata. Keith, you may now end the call.

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Operator

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

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