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ST.N - Q1 2025 Sensata Technologies Holding PLC Earnings Call

EVENT DATE/TIME: MAY 08, 2025 / 8:30PM GMT

OVERVIEW:

Company Summary

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PRESENTATION

Operator

Good afternoon, and welcome to the Sensata Technologies first-quarter 2025 earnings call. (Operator Instructions) Please note that this event is being recorded.

I would like now to turn the conference over to Mr. James Entwistle, Senior Director of Investor Relations. Please go ahead.

James Entwistle - *Sensata Technologies Holding PLC - Senior Director of Investor Relations*

Thank you, Jason, and good afternoon, everyone. I'm James Entwistle, Senior Director of Investor Relations for Sensata, and I'd like to welcome you to Sensata's first-quarter 2025 earnings conference call. Joining me on today's call are Stephan Von Schuckmann, Sensata's Chief Executive Officer; and Brian Roberts, 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 conference call. The PDF of this presentation can be downloaded from Sensata's Investor Relations website. This conference call is being recorded, and we will post a replay 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 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 filings with the SEC.

We encourage you to review our GAAP financial statements in addition to today's presentation. Most of the information that we will discuss during today's call will relate to non-GAAP financial measures. Our GAAP and non-GAAP financials including reconciliations, are included in our earnings release, the appendices of our presentation materials, and in our SEC filings.

Stephan will begin the call today with comments on the overall business. Brian will cover our detailed results for the first quarter of 2025 and our financial outlook for the second quarter of 2025. Stephan will then return for closing remarks. We will then take your questions.

Now I would like to turn the call over to Sensata's Chief Executive Officer, Stephan von Schuckmann.

Stephan von Schuckmann - *Sensata Technologies Holding PLC - Chief Executive Officer*

Thank you, James, and good afternoon, everyone. Let's begin on slide 3. We delivered a strong first-quarter 2025 with revenue, adjusted operating income, and adjusted earnings per share, all exceeding the high end of our guidance. We are pleased with these results especially given the volatile and constantly evolving tariff environment, which continues to have daily impacts on key end markets.

I want to thank our customers, suppliers, and our Sensata team for their efforts to work through unprecedented levels of change and uncertainty to deliver what I expect is the first of many strong quarters during my tenure. While I know tariffs are top of mind for many, I'd like to start the call today by going a little deeper on the three strategic imperatives that I shared earlier this year. These key pillars of improving our operational performance, optimizing our capital allocation, and returning Sensata to growth from our priorities and our core areas of focus.

Much of my initial 100 days with Sensata have been spent observing, listening, and learning, and I've traveled to our factories, spent time with our teams, and met many of you, our shareholders. I've watched how we manufacture and deliver our products, how we innovate and plan for future growth by winning new business opportunities, and have begun the process of taking a fresh look at our strategy. These efforts resulted in some key observations on which we're already taking action to drive progress on these pillars.

And we start with improving our operational performance. Last quarter, I clearly defined what it means to be operationally excellent, but it's important and warrants repeating. Operational excellence is not just about cost productivity and margin percentage, it means delivering a high-quality product to our customers on time at the lowest possible cost while we efficiently manage production capacity and optimize inventory levels. It also requires us to be excellent across all areas of our organization.

While manufacturing and production are at the forefront, we also strive to be best in class in our commercial, procurement, SG&A, engineering, and innovation teams. To ensure we are setting the right levels of ambition across the company, we are now continuously benchmarking Sensata internally and externally to remain the supplier of choice for our customers, affording us the opportunity to win new business and gain share.

While Sensata is top quartile margins, the work we have done over my first 100 days has made clear that we have exciting opportunities to improve the pursuit of operational excellence. Over the last two decades, I've experienced what best-in-class lean manufacturing looks like, and I know that we have untapped potential to leverage our strong teams at Sensata. Let me dive a little deeper and give you some examples.

First, consistency in operations. As I traveled to our factories, it was apparent that each location does certain things differently at Sensata rather than following a standardized production system. This results in sites implementing different standards from line concepts to floor management, leading to the same components being produced at various varying cost levels. We want all our factories producing the same component at the lowest possible cost. To achieve this, we're implementing a standardized production system, much like the various derivatives of the Toyota production system adopted across the auto industry.

Second, continued focused on inventory management. Our team made good progress in 2024, reducing absolute inventory dollar levels by nearly \$100 million or 14%, but we see opportunity to improve working capital, optimizing our inventory further. To enable this, we have kicked off a new initiative focused on integrated supply chain planning to gain a more accurate planning of part level demand integrated through production and materials.

Third, a more strategic approach to procurement. Over the past few years, our procurement organization became more tactical in adjusting to a highly inflationary environment, including working diligently over the last year to recover much of the cost increases that have absorbed during the worst of those inflationary times. While this certainly positioned us better than we otherwise would have been, we have not invested sufficiently to develop our suppliers to drive the same or better levels of productivity improvement through the supply chain. Accordingly, we have reorganized our operations group to allocate resources to supply development and improvement programs. These changes will increase our operating resiliency in 2025 and beyond. The savings we derive will enable us to embark on additional initiatives setting the foundation to continue to expand margins.

Let me now turn to my second pillar, capital allocation. Our focus here is simple. To ensure that we are effectively allocating capital to maximize return for our shareholders. The Board and I take this responsibility to invest our shareholders' cash seriously. We are committed to meaningful improvement. And the first step is to increase free cash flow conversion.

We've made great strides in free cash flow conversion in the first quarter, and our conversion rate improved by 26% points year over year to 74%. Given the strong Q1 result, we used approximately \$100 million of cash to repurchase 3.5 million shares. We are confident in our ability to improve free cash flow and expect to follow the disciplined approach we took last year by returning cash to our shareholders through share repurchases, reducing our net leverage, and maintaining our current level of dividend.

Finally, let me speak to returning Sensata to revenue growth. Over the medium and long term, to be able to better understand our opportunity for growth, I've spent considerable time these last few months diving deep into our product innovation, our ability to attract and win new business, and our overall positioning within our markets. Product innovation is critical, and we are seeing exciting opportunities across our portfolio to innovate and drive value for our customers. We've spent considerable time over the last several quarters discussing our leak detection sensing capabilities in the HVAC space.

Our industrial business is a clear leader in this new market segment and remain enthusiastic that this will be a growth driver for Sensata over the next several years. The breadth and depth of our ICE and electrification technologies are core strengths for Sensata across our auto and HVR businesses. We are well positioned to be the supplier of choice across areas such as braking, emissions, and electrical protection, and we are winning business in all regions.

As an example, in the first quarter, we booked a significant win in Japan with Mazda for exhaust and fuel sensors. This follows important wins in 2024 with Toyota and other Japanese OEMs as we continue to make significant strides in this market. In China, we successfully secured several contractor and TPMS business awards with market leading local EV OEMs as well as significant wins through leading local tiers serving the global market. These wins demonstrate our capability to compete and win around the world. As we look out to 2026 and 2027, we're excited about further growth opportunities from our portfolio of high-quality products.

Now I'll take a moment to discuss how we manage tariffs. Let's turn to slide 4. The direct and indirect effects from tariffs are the primary issue impacting us, our customers, and our end markets today. Over the last decade, we have positioned ourselves well by proactively focusing on a region-for-region strategy to align our supply chains and production with our customers. North America represents approximately 40% of our global revenue, of which we serve roughly 70% from production in Mexico.

Since early March, when the 25% tariff on non-USMCA qualified components from Mexico took effect. We have been working diligently with our customers to minimize the impact of tariffs to their business and ours. For example, in early March, less than 50% of our products manufactured in Mexico were USMCA qualified. Our team has worked tirelessly to improve this, and today, 80% of our revenue sourced from Mexico is now USMCA qualified.

We're working with customers to leverage our global footprint to deliver tariff mitigation solutions such as changes to logistics, production, and sourcing. When we must incur tariff costs to supply our customers, our position is clear. Our customers must absorb these incremental costs. To effectuate this outcome, there have been an ongoing dialogue with our customers to secure their agreement to reimburse tariff costs. As today, we have mitigated more than 95% of our gross tariff exposure in our auto and HVR business through a combination of tariff exemptions, customer agreements to reimburse tariff costs, and various other actions.

Finally, let me take a moment to discuss the ransomware incident at Sensata in early April. The incident temporarily impacted our operations to varying degrees over roughly two-week period. Thanks to the exceptional work of our operations, customer service, and IT teams as well as a team of third-party cybersecurity professionals, we're happy to report that we are back to normal business operations.

And let me turn the call over to Brian to provide greater detail on Q1 and our thoughts around the second quarter and full year.

Brian Roberts - Sensata Technologies Holding PLC - Chief Financial Officer, Executive Vice President

Thank you, Stephan. Good afternoon, everyone. For clarity, unless noted, all amounts are denominated in US dollars. Let me start on slide 6.

As Stephan noted, we delivered a strong first quarter, despite the macro uncertainty in our end markets, with revenue, adjusted operating income, and adjusted earnings per share all ahead of expectations. We reported revenue of \$911 million for the first quarter of 2025 compared to revenue of \$1.007 billion in Q1 of 2024. Adjusting for the actions we shared last year to divest \$200 million in annualized revenue related to various low-margin, low-growth products, and the Q3 2024 sale of INSIGHTS, revenue was approximately flat year over year and up sequentially 1%. Past revenue related to tariffs recorded in Q1 was negligible at approximately \$2 million.

Adjusted operating income was \$167 million, representing a margin of 18.3%, consistent with our expectations. While this denotes a year-over-year decrease of about 40 basis points, it is, as expected, given a return to a more normalized seasonality pattern of margins related to the timing of pricing and productivity. Excluding approximately \$2 million of net cost impacts from tariffs, our adjusted operating margin for Q1 would have been 18.6% above our guidance range. Stephan has made quite clear that our expectation is to pass through tariff costs to our customers. However, there may be some minimal quarterly impact due to the timing gap between tariff payment and cost recovery.

Adjusted earnings per share in the first quarter of 2025 was \$0.78 compared to adjusted earnings per share of \$0.89 in Q1 2024. The Q1 2025 result exceeded the midpoint of our guidance by \$0.07 or about 10%. This result was due to a combination of our strong operational performance, lower-than-expected taxes incurred, and the repurchase of approximately 3.5 million shares during the first quarter, reducing our overall shares outstanding.

Now let's turn to slide 7 to discuss segments. Sensing solutions, which is comprised primarily of our industrial and aerospace businesses, delivered \$261 million of revenue in the first quarter of 2025, up 3% year over year after adjusting for the various divested products. Stability across industrials and aerospace, combined with our growing A2L gas leak detection sensing products contributed to the positive Q1 result. This is the first period where we have seen year-over-year growth in sensing solutions since the second quarter of 2023. While we remain cautious in our outlook given the uncertain macro environment, we are encouraged by this progress. Sensing solutions' operating margins was 29.2% in the quarter as compared to 28% in Q1 2024 as a result of operating efficiencies and improvements to the product portfolio.

Performance sensing, which includes our automotive and heavy vehicle off-road businesses, reported revenue of \$650 million in the first quarter of 2025, a decrease of about 9% year over year or about 8% after adjustment for divested products. We slightly undergrew the market in Q1 in auto given our previously discussed mixed issues in China as well as volatility in European OEM production schedules driven by shifts in the regulatory outlook. This was partially offset by increased North American production ahead of tariffs for parts that were USMCA qualified. We continue to expect that outgrowth will normalize in the second half of 2025 as we lap the China year-over-year comparisons and see improved regulatory clarity in Europe.

HVOR orders slowed more than initially anticipated in Q1, corresponding to the weaker market outlook for this segment as tariffs and regulatory shifts impact customer demand. Performance sensing adjusted operating margin was 22% in Q1 as compared to 23.7% in Q1 2024, as we return to normal seasonality and timing of pricedowns offset by productivity gains. Corporate and other has been recast to exclude certain costs previously referred to as megatrend spend which are now presented within the two reporting segments. Adjusted corporate operating expenses were \$52 million in the first quarter of 2025, a decrease of approximately 10% or \$6 million versus the first quarter of 2024, reflecting efficiencies gained because of the restructuring efforts taken in the second half of last year.

Turning to slide 8. Stephan noted we remain laser focused on improving our free cash flow conversion, and I'm pleased that we continued our momentum in the first quarter. Free cash flow conversion improved 26 percentage points year over year to 74% in the first quarter as compared to 48% in Q1 2024. Free cash flow is \$87 million, up 35% from \$64 million in the same quarter last year. This strong Q1 result sets the foundation for Sensata to further improve free cash flow conversion in 2025 as compared to 2024.

Net leverage in the first quarter was just above 3 times. This was as planned due to a lower trailing 12-month EBITDA denominator caused by the sale of INSIGHTS and the divested products. We were proactive around share repurchases in the first quarter, buying approximately 3.5 million

shares for approximately \$100 million of cash. In addition, we returned \$18 million to shareholders in the first quarter through our quarterly dividend and have approved our second-quarter dividend at the same \$0.12 per share rate payable on May 28th to shareholders of record as of May 14th.

These capital deployment actions yielded an improvement in our return on invested capital of a half point as ROIC increased to 10.2% for the 12 months ended March 31, 2025 as compared to 9.7% for the 12-month period ended March 31, 2024. Building upon Stephan's earlier comments, I'd now like to provide a brief overview of our current tariff exposure. Our tariff considerations primarily fall into three main categories: exposures related to products produced in Mexico, exposures related to the escalated tariff rates between the US and China, and exposure related to the potential for increased costs for reciprocal tariffs. Currently, we are not exposed to tariffs specific to auto parts as our products are not in scope.

Now let me take a moment to talk about each of these exposure categories. First, Mexico. As we've discussed, approximately 70% of our North American production is imported from Mexico to the US. Currently, approximately 80% of that Mexico source revenue qualifies under USMCA and is not subject to tariffs. For other parts, we are working with our customers to help mitigate the cost by identifying alternative means of delivery, leveraging our global footprint, or pursuing alternative sourcing of materials. If no other options are available, we have been clear that our customers must absorb this cost.

The escalation in rates between China and the US has two main impacts on Sensata, as between 5% and 10% of our core industrial revenue or 1% to 2% of total Sensata revenue is subject to these tariffs. In many cases, starting in the second quarter, distributors are putting some orders on hold awaiting potential reduction in the current rates, which range up to 145%. We are hopeful that in the coming months, China and the US will reach an updated trade agreement, reducing these rates and allowing us to ship these products. In advance, we have produced the required inventory such that if an agreement is reached, we will quickly be able to fulfill customer demand.

The second exposure is related to certain raw materials that we source from the US into China for products produced in China. For these raw materials, we are working on alternative sourcing and delivery options to mitigate this risk.

Finally, regarding the reciprocal tariffs, we will continue to monitor this closely over the next few months, as elevated future tariffs in markets where we operate may restrict our ability to leverage our global footprint as efficiently as possible. Currently, reciprocal tariffs do not have a material impact on our business. Given the various executive orders in effect as of today, we anticipate incurring approximately \$20 million of tariff costs in the second quarter. We expect to be able to offset this cost through incremental billings to customers and pricing actions to distributors. The end result should effectively be a net \$0 impact to adjusted operating income.

Turning to slide 9, we note that third-party auto production estimates were revised downward significantly in April by 1.6 million units over the remainder of 2025, with most of the decline attributable to North America. For the second quarter, the global expectation is down 2%, with higher degrees of volatility by region, including Europe and North America, down 6% and 10% respectively, while China remains strong.

As we build our guidance expectation for Q2 and our thoughts for the second half of the year, we are aligning with these updated third-party estimates. We've also considered the incremental risk in industrial related to the China and US tariffs. In summary, the team is doing an outstanding job to mitigate tariff risk wherever possible and ensure that any tariffs incurred will be offset by increased pricing or passed through billings.

Let me now turn to slide 10 to discuss our guidance for the second quarter of 2025 and provide some additional thinking for the second half of the year. We currently expect revenue of \$910 million to \$940 million for the second quarter. This includes an expectation of approximately \$20 million in tariff passed through revenue. Adjusted operating income for the second quarter is expected in the range of \$169 million to \$177 million and is not expected to be impacted by tariffs, as any expense incurred would be offset by the pass-through tariff revenue. However, zero margin passed through revenue will have a dilutive effect on adjusted operating margin index of about 40 basis points.

Including approximately \$20 million in tariff revenue, we expect an adjusted operating margin index range of 18.6% to 18.8%. Again, for clarity, if we exclude approximately \$20 million of anticipated pass-through tariff revenue in the second quarter, we would expect revenue of \$890 million to \$920 million, adjusted operating income unchanged at \$169 million to \$177 million, and an adjusted operating margin index range of 19% to 19.2%. For the second half of 2025, we are preparing for the more significant cuts in automotive production currently forecasted by third-party

sources, which are highly concentrated in North America. This will likely impact revenue by about \$20 million to \$30 million per quarter in each of Q3 and Q4.

At this level of revenue decrease, we remain confident in our ability to expand our pre-tariff adjusted operating income margins by approximately 20 basis points per quarter over the course of the second half of the year. Like all of you, we are watching the macro environment closely for further regulatory and economic changes, and we'll continue to update our expectations accordingly.

With that, I'd like to turn the call back to Stephan for closing remarks.

Stephan von Schuckmann - *Sensata Technologies Holding PLC - Chief Executive Officer*

Thank you, Brian. Before we move to Q&A, I'd like to leave you with some closing thoughts. What I outlined today is a glimpse into the significant transformation underway at Sensata. While we are still in the early days, I can state with confidence that after my first 100 days in the role, I'm even more optimistic than I was on day one. The foundation of the business is solid with much to build upon. We're developing a high performance organization and creating a culture of continuous improvement, and we are taking a benchmark-driven approach towards setting ambitious goals across all regions, functions, and product families. I'm confident that the work we are doing here is creating a level of resiliency in our business that will continue to deliver meaningful results in the short term and in the future.

Finally, with regard to tariffs, thanks to the extraordinary work of our Sensata team and the collaborative approach from our customers and suppliers, we have now mitigated substantially all of our current tariff exposure.

With that, I'll turn the call back to James. Thank you.

James Entwistle - *Sensata Technologies Holding PLC - Senior Director of Investor Relations*

Thank you, Stephan and Brian. We will now move to Q&A. Jason, please introduce the first question.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Wamsi Mohan, Bank of America.

Wamsi Mohan - *Bank of America-Merrill Lynch - Analyst*

Yes, thank you so much, and thanks for all the color around around tariffs. It's super helpful. I was wondering if you could help us think through your comment, Brian, on the second half impact of \$20 million to \$30 million per quarter in Q3 and Q4. How much of that is related to straight production cuts versus potentially outgrowth trends? And maybe you can just help us think through those moving pieces as you as you think about the total revenue impact in the second half.

Brian Roberts - *Sensata Technologies Holding PLC - Chief Financial Officer, Executive Vice President*

We're basically making it 100% really on straight production cuts. So if you look at North America, which is forecast to be down somewhere between 500,000 and 600,000 units per quarter in Q3 and Q4, that's the real driver of the change as we look through the production expectations into the second half. We thought it prudent to be able to make sure that we were adjusting for it now.

Wamsi Mohan - Bank of America-Merrill Lynch - Analyst

And if I could quickly follow up, the sensing solutions growth that you saw, would you say any of that is attributed to any pull forward impact and demand that certain markets have seen because of tariff reasons?

Brian Roberts - Sensata Technologies Holding PLC - Chief Financial Officer, Executive Vice President

Yeah, I'll start, and then, Stephan, if you want to jump in. From my perspective, no, we hadn't really seen much in tariff impact in industrials especially in the first quarter. As we talked about last quarter when the when the tariff rates in China were roughly about 20%, it just wasn't material to the business. Obviously, there has been escalations of that since, which happened late in the quarter into early Q2, so really didn't see anything that happened from a pull-in perspective there.

If anything, as those rates have escalated, we have seen some things be put on hold here in Q2. And hopefully, again, if we can find a more reasonable compromise between the two countries, then we're certainly prepared to ship as soon as customers give the okay to release those orders.

Stephan von Schuckmann - Sensata Technologies Holding PLC - Chief Executive Officer

And I think what I could add, Wamsi, we're making good progress on our gas sensing leak detection. And we've launched our A2L product range. And what you're seeing is the first level of growth impact. And that's basically one of the impacts of this growth within the industrial sector.

Operator

Mark Delaney, Goldman Sachs.

Mark Delaney - Goldman Sachs - Analyst

Yes, thank you very much for taking my questions. And thank you for all the details on your key priorities, Stephan, and also the tariff exposure.

Stephan, you mentioned in your prepared remarks progress in Asia with some Chinese local EV OEMs and also with some Japanese auto OEMs, and those are two customer sets that have historically been smaller for Sensata. Can you help us better understand the size and scope of the wins thus far? Would you consider the bookings, so far, as still small but a good start to build on, or do you think the awards you already have will ramp to a meaningful level of revenue for the total company?

Stephan von Schuckmann - Sensata Technologies Holding PLC - Chief Executive Officer

So I'll explain it like this, Mark, and first of all, thanks for your question. We've made good progress in China. The team has been very active in Southeast Asia, specifically in Japan. And those are the wins that I've mentioned around Mazda and with Toyota that we've won last year. I think it's important to say that we've also made good progress especially in the EV sector in China, and it's pretty broad.

So the team has not only won business with international OEMs, being successful in China, but specifically also with Chinese OEMs. So we've had wins with local OEMs and in all different product areas.

Mark Delaney - Goldman Sachs - Analyst

Okay, and just, I mean, as you think about what you've actually booked so far, I mean, are they still relatively small in terms of the revenue they'll represent over the next few years as they ramp up, or are these already pretty large?

Stephan von Schuckmann - *Sensata Technologies Holding PLC - Chief Executive Officer*

No, these are, I would say, small- to medium-sized, so it's still pretty small overall but growing step by step. So we've made some good improvements but medium to small wins.

Mark Delaney - *Goldman Sachs - Analyst*

My other question was around EBIT margins. The company had been anticipating EBIT margins for the year in the low 19% range. You're off to a good start based on what you spoke to for your expectations in the first half. But Brian, I believe you talked about some margin expansion in 2H even on lower revenue, but could you speak a little bit more on your updated margin expectations for the year, in particular as you think through any effects from tariffs and some of those revenue trends that you spoke to?

Brian Roberts - *Sensata Technologies Holding PLC - Chief Financial Officer, Executive Vice President*

Yeah, absolutely. So again, I mean, we're obviously going off the information we have currently, right? So I want to make sure that we're all clear that we're using April IHS effectively or S&P Global mobility for effectively some of the production data. And as we know, that may be volatile, so we'll obviously have to continue to update for that. But as we sit today, we felt very good about our Q1 result, again excluding -- yeah, we wound up with a couple million dollars of net impact on tariffs in the first quarter.

A lot of that, quite candidly, with things that were in transit when tariffs were first announced, and we couldn't turn things around or so in time. That's really kind of a one-time effect. If you excluded that out, we would have been 18.6% in Q1, which would have been a very strong result.

As we're looking, again, excluding tariffs here as we talk about going forward, Q2, we certainly still expect to be back into the 19%-plus range, and then we're stair stepping very similar to how we did last year in Q3 and Q4. So I think if you blend that all together, what we said last quarter still holds true that we think we're at or above where we were for 2024. So we're encouraged by that.

Certainly, a lot of the initiatives that Stephan's talking around about to be able to become more operationally excellent, those initiatives are going to help us. Certainly, they can help us a little bit here in the back half of '25, but then they'll also start to set the table for us in '26. So we're certainly excited about that progress and what it's going to be able to do for us to hopefully continue this margin expansion kind of run, if you will, going forward.

Operator

Joe Giordano, TD Cowen.

Joseph Giordano - *TD Cowen - Analyst*

Brian, not to pin you down too much, but is the \$20 million to \$30 million of like the incremental production costs, like is that being offset elsewhere like industrial starting to grow again? Obviously, you get the tariff revenue, but like just trying to square like that.

We're not saying that revenue is down \$20 million to \$30 million. It's just there is an impact that needs to be filled. Is that how we should think about it?

Brian Roberts - *Sensata Technologies Holding PLC - Chief Financial Officer, Executive Vice President*

Yeah, I mean, again, from where we were three months ago when we started to talk about color for the full year, we've seen 1.6 million auto units effectively come out with the great majority of those being in North America and then another slug in Europe, right? And so when you look at that, that's just that many less light vehicles that are going to get produced that has an impact on the business. So we've quantified that, looking at roughly, again, North America being down 5000,000 to 600,000 units per quarter for Q3 and Q4, and roughly, that's \$25 million plus or minus of revenue impact to us.

I think the rest of the business, obviously there can be risk that comes with the tariff exposures of just around production levels. But overall, I think especially on the sense exclusion side, we feel very good about the progress and momentum we've made. So again, we may see some distributor orders put on hold here in Q2 due to the tariff uncertainty, but we're working our way through that and the underlying foundation seems very solid.

Joseph Giordano - *TD Cowen - Analyst*

And then on the ability to feel that good about margins despite that headwind in the US on profitable business, what are like the main buckets that's helping you and giving you that visibility? Is it like head count and issues that have already happened, where are you pulling those levers?

Brian Roberts - *Sensata Technologies Holding PLC - Chief Financial Officer, Executive Vice President*

Yeah, I mean, we're -- I mean, I would say this is all really coming right now from operational productivity, right? So I mean, as we built our plan for '25 of where we were going to see growth, how we're going to kind of work our way through the productivity, mass, if you will, to offset pricing and other things, the teams have done a really good job of minimizing pricing impacts where possible, being able to continue to drive procurement, continue to drive just overall efficiency. We're getting some of the benefits now from some of the restructuring charges that we took in the back half of '24. All of those things are leading to, I think, giving us more confidence in our margin plan moving forward.

Operator

Joe Spak, UBS.

Joseph Spak - *UBS - Analyst*

Brian, I guess just going back to your comments on the back half. I mean, I understand what those third-party providers did. I would argue increasingly that's looking pretty conservative based on some other commentary we've gotten from companies. So I mean, if that doesn't happen, I'm just doing some quick math, but like it would suggest that maybe that quarter per margin finish could be 5 to 10 basis points better than you indicated. Is that about right?

I just want to sort of calibrate for potential upside if sort of that case doesn't play out.

Brian Roberts - *Sensata Technologies Holding PLC - Chief Financial Officer, Executive Vice President*

I'm going to hold off on trying to recalculate on the margin side because obviously, if global production numbers are improved in the back half of the year as the tariff environment eases, for example, then, we're certainly prepared to take advantage of that when that happens, right? So where we can only go off of the data we have and, man, I'm really bad at predicting the lottery numbers. But that's kind of how we're thinking about it.

Joseph Spak - UBS - Analyst

Fair enough. And just on the tariff, so the -- I understand you expect to sort of be fully compensated for that. Has that already, like what percent of that has already been negotiated? How much is still in progress that needs to be done?

Brian Roberts - Sensata Technologies Holding PLC - Chief Financial Officer, Executive Vice President

Yeah, no, sorry, go ahead.

Stephan von Schuckmann - Sensata Technologies Holding PLC - Chief Executive Officer

So basically, we've had, a broad range of negotiations with, I would say, all of our customers, in the HVOR sector and also in the auto sector. And as I mentioned, we've basically covered 95% through -- managed to mitigate 95% of the risk with these negotiations, through these negotiations.

Brian Roberts - Sensata Technologies Holding PLC - Chief Financial Officer, Executive Vice President

So if you want to put that into dollar terms, Joe, right, if we're booking \$20 million of of tariff roughly in Q2, we're talking about \$1 million worth of exposure still to cover.

Joseph Spak - UBS - Analyst

Okay. And then just, Stephan, now that you've had a little bit more time and appreciate your three pillars update, just wondering if you have any more thoughts on the Sensata portfolio, whether there's any holes that you see, any other areas you think the company may be able to win, or maybe some products that upon further review might not be core?

Stephan von Schuckmann - Sensata Technologies Holding PLC - Chief Executive Officer

So look, the focus in these first 100-plus days has been on these three pillars. So it has been on operational performance, and I've been focusing a lot around growth and everything else that I've mentioned so far. And, yes, of course, I'm looking at the portfolio. I'm looking in industrials. I'm also looking at the portfolio in auto. But up to date, there's no change to that at this point in time.

Operator

Christopher Glynn, Oppenheimer.

Christopher Glynn - Oppenheimer - Analyst

I want to touch on the first pillar that Stephan articulated and, Brian, you talked about setting the table for continued progress in '26. Just curious if that comment reflects an expectation of kind of cumulative organizational builds. I know it's early days, but in terms of the vision, would this be anticipating some acceleration in the margin pacing by the time we phase into '26 or more about sustaining a steady moderate pace over time?

Brian Roberts - Sensata Technologies Holding PLC - Chief Financial Officer, Executive Vice President

Just trying to get through Q2 here, Chris. Yeah, I think too early to tell, right? I mean, as we work through '26 planning in the back half of the year, we'll obviously have a lot more visibility and understanding around the environment. We'll certainly have a lot better visibility and understanding

around kind of how we think about pricing for next year, and a lot of these initiatives that Stephan has kicked off with the teams and really trying to drive this concept of a standardized production system and operational excellence.

So I put that into the more to come category at this point, but certainly doing the things necessary now to give ourselves the best chance for further expansion going forward.

Stephan von Schuckmann - *Sensata Technologies Holding PLC - Chief Executive Officer*

And let me add to that, I think we've mentioned it's one of our times, we've got a lot of changes, we've got a lot of things that are unpredictable. So everything that we're doing at this point in time to try and improve operational performance with the examples that I've given is to be more resilient against these impacts that that might come or might not come.

Christopher Glynn - *Oppenheimer - Analyst*

Yeah, I appreciate it. It's early days, and it was just meant the internals in isolation, but appreciate it's early days and stay tuned for more to come. Brian, I assume the 20 basis points sequentially through the back half on the margin, that assumes the \$20 million zero margin pass through is static?

Brian Roberts - *Sensata Technologies Holding PLC - Chief Financial Officer, Executive Vice President*

Yeah, I mean, think of the numbers as kind of pre tariff, right? So, I mean, I think it's -- it'll be good practice for us so we can kind of stay apples to apples given that clearly the the tariff environment is volatile, and we'll probably continue to change each quarter. We'll continue to look at this kind of inclusive of tariff and then excluding tariff as well and give you both sets. But when we talk about 19 and 19.2 here in Q2, which is what we talked about last quarter, that's obviously excluding the tariffs and then 20 basis points plus or minus in Q3 and Q4, you can stair step that really on both, I guess.

Christopher Glynn - *Oppenheimer - Analyst*

Got it. Okay. And then on aerospace, your last couple quarters, most vendors, at least that we cover and follow have had negative OEM revenue. You talked about stable. That stables like a point in time in a long-term growth path for production. Do you see that pivoting back as the OEM and the supply chain alignment? I think a lot of companies have talked about it back to growth after the March quarter. So wondering if you're anticipating a pivot in the year-over-year revenue performance for aero.

Stephan von Schuckmann - *Sensata Technologies Holding PLC - Chief Executive Officer*

I mean, I could say a few words. No, we don't see that. We see a strong development within our aerospace business. And we also expect a certain level of growth within 2025. But I'll pass on to Brian to say a few more detail.

Brian Roberts - *Sensata Technologies Holding PLC - Chief Financial Officer, Executive Vice President*

Yeah, no. I think that's exactly right. I mean, it's some -- obviously certain customers have had some challenges in the aerospace area, but as those continue to resolve themselves, that bodes well for us. I think we have a very strong backlog in aerospace. And so we'll continue to show, I call it, kind of steady Eddie growth in aerospace both on the revenue side as well as on the margin profile.

Stephan von Schuckmann - *Sensata Technologies Holding PLC - Chief Executive Officer*

And our large customers, as you know, have good and solid backlog on which we can build and grow.

Operator

Samik Chatterjee, JPMorgan.

Samik Chatterjee - *JPMorgan - Analyst*

Maybe if I can start with the second half color that you provided on the automotive volume sort of risk or the downside from a third party forecast perspective, can you share any primary view here in terms of a similar, either sort of changes in third-party forecast or your thinking at this stage relative to the heavy truck market and maybe to the extent that you can on the industrial side how the second half looks? But interested in seeing if you are -- if you have any thoughts in relation to sort of the risk from the macro in terms of those two areas, and I have a follow up.

Brian Roberts - *Sensata Technologies Holding PLC - Chief Financial Officer, Executive Vice President*

Yeah, sure, Samik, I appreciate the question. Let me give you a little color. So yes, you're right, auto obviously easy to track just using third-party data there. And, look, I mean, I hope that, Joe's -- back to Joe's question, he was right that it ultimately proves a little conservative, and that would be a good thing for all of us.

When we think about HVOR, that market outlook has clearly also worsened over the course of the last couple of months in this tariff environment. We've seen weakness in on-road truck. I think some of the pre-buy that people expected to have come through due to potential regulatory changes around emissions and other things in the US likely being delayed, then coupled with the tariff environment, I think it certainly slowed any of those production expectations around pre-buy. Yeah, we've worked that into the model.

On the industrial side, again, we've got three quarters in a row now of what I call at least good solid stability there. We'll have to watch for if the demand environment changed a little bit due to the tariffs, especially if China and the US can't reduce the rate that they're charging each other at the moment. But I think everybody's still hopeful that that will resolve itself here in the coming periods.

And the outlook, I think, in our industrial business is, I'd say, solid. I don't want to get too far over our skis on it, but I think it has certainly been improving.

Samik Chatterjee - *JPMorgan - Analyst*

Okay, got it, and then just in relation to the wins that you mentioned in your prepared remarks and obviously it's a pretty uncertain macro, so when you sort of are now looking at the pipeline of activity and engagement with customers, are you seeing any, and I'm referring to automotive customers, are you seeing any push outs in terms of maybe the timelines of when you expect customers to decide on some of these engagements and wins, how they translate or how quickly they translate into wins? Are you seeing any changes on that front just given that they have multiple other things to now take care of, I guess?

Stephan von Schuckmann - *Sensata Technologies Holding PLC - Chief Executive Officer*

I think I'd answer that question twofold. So we've seen both. On the one hand, we've seen customers pushing out projects and postponing projects especially around electrification. But on the other hand, depending on the region that you're in, we see customers that are extremely bullish especially around China and especially around EV platforms and applications. We see actually an acceleration of projects and basically no cancellations. So it's two-folded, depending on what region you look at.

Operator

Shreyas Patil, Wolfe Research.

Shreyas Patil - Wolfe Research - Analyst

Maybe just starting on sensing solutions. So you know that the business has returned to growth here. Just wondering how we should think about the incremental margins in that business, assuming we can maintain further revenue increases.

Brian Roberts - Sensata Technologies Holding PLC - Chief Financial Officer, Executive Vice President

So I mean, clearly, if you go back to the segment numbers that we gave, which is in the slide deck and in the queue, good strong operational margin improvement year over year. We'd expect that trend to continue here over the next couple of quarters, certainly a contributor to how we're thinking about the incremental margin expansion we're talking about for Sensata in total given the outlook within that group as compared to a tougher environment on the auto and HVOR sides.

Shreyas Patil - Wolfe Research - Analyst

Okay, and maybe just following up on the last question because, I believe, for 2026, the plan, or at least the expectation was for a pretty significant increase in EV launches in Europe. So should we be assuming that those programs are getting pushed out or delayed, or is that just a reference to what you're seeing over the next few quarters?

Stephan von Schuckmann - Sensata Technologies Holding PLC - Chief Executive Officer

No, I don't see those programs being pushed out. In the contrary, I mean, most of the OEMs need to reach their CO2 targets. And within the mix of the total production volumes that they have, they need to have a certain level of EVs. So what we're seeing here in our view is actually projects being launched or products being launched one after the other.

And I think '26 and partially 2025 is a year where we are now seeing especially the second generation of electric vehicles being launched. So those are predominantly vehicles on 800-volt platforms with a higher range and higher charging speeds. So I don't think that those vehicles will be pushed out because they're technologically on the highest level, and I could expect that OEMs want to get these vehicles into the market because there'll be a higher end customer acceptance in comparison to first-generation vehicles.

So to be precise on your question, Europe wouldn't see much pushouts anymore. In the contrary, I think they will be launched step by step. The pushouts were related to projects previously launched.

Operator

Kosta Tasoulis, Wells Fargo.

Kosta Tasoulis - Wells Fargo - Analyst

I want to talk about free cash flow and now another strong quarter of that. Brian, are all the levers that you -- the kind of the low hanging fruit that you can pull to improve free cash flow kind of already done, or is there any -- can you talk about maybe any other levers that are remaining to pull?

Stephan von Schuckmann - *Sensata Technologies Holding PLC - Chief Executive Officer*

Let me take the first part of that question, and then I'll pass on to Brian. Look, I think, improving your free cash flow and the example that I mentioned especially around inventories is something you need to continuously work on, and that's what we're doing. So I wouldn't call it a low-hanging fruit, but I think it's something that you can improve step by step and make significant gains throughout 2025 and even beyond that, and that will drive a certain level of free cash flow improvement. But there are also other levers.

And then I'll pass on to Brian.

Brian Roberts - *Sensata Technologies Holding PLC - Chief Financial Officer, Executive Vice President*

Yeah, I mean, I think we've obviously made significant progress year over year. From '24 to '23 was 25, 26 percentage points and continued that in Q1. Q1 is notoriously probably the most challenging quarter to grow cash. I absolutely agree with what Stephan just said. I think there's still a significant opportunity for us in the area of inventory.

I do think we'll see a few ebbs and flows on that. I mentioned before, we're building a little bit of inventory in our industrial area right now, assuming at some point this distributor demand is going to get released and we didn't want to get caught flat-footed on that. We want to be able to ship quickly. So yeah, there can be slight ebbs and flows from a period to period, but overall, absolutely I think the trend is still pointing in the right direction, and we have more growth and more improvement to get in the area of cash flow.

Stephan von Schuckmann - *Sensata Technologies Holding PLC - Chief Executive Officer*

And let me add one more point to that. We're challenging ourselves, so I think we've made good progress just as Ryan mentioned. But we're looking outside of Sensata, and we're looking at peers and competitors out there. And we're looking who's really good, for example, in days on hand in inventory and in overall inventory levels. And we're comparing ourselves to that, and we're doing that in every region and through every plant. And we see certain levels of opportunities within that.

Kosta Tasoulis - *Wells Fargo - Analyst*

That's great guys. And then speaking of competitors, would you able to provide any color on how your manufacturing footprint compares to your competitors? You mentioned you improved your USMCA compliance. Can you talk about how your position is relative to them and if that could be possibly the opportunity for you?

Stephan von Schuckmann - *Sensata Technologies Holding PLC - Chief Executive Officer*

Look, I think Sensata has a very competitive manufacturing footprint. The teams around production have done a fantastic job, first of all, in scaling up production and basically being very local for local. I think that is a strength of Sensata. I think the opportunity within production lies within the productivity of each facility. So when we look out at our competitors, yes, of course, we look at manufacturing footprint.

But what we do, what we especially look at is the productivity levels that we're on. And we look at what's best in class around productivity. And that's why we benchmark ourselves, and we strive to be better. And that's one of the initiatives that we're working on this year, and we'll also be working on through 2026 to get us onto that next level of productivity. That's our target.

Operator

Guy Hardwick, Freedom Capital Markets.

Guy Hardwick - *Freedom Capital Markets - Analyst*

Stephan, just wondering based on the pillars of that you target that whether you have a sense for what you think the long-term margin potential of the business is, bear in mind what you said about second-generation EVs in 2026.

Stephan von Schuckmann - *Sensata Technologies Holding PLC - Chief Executive Officer*

Look, Guy, I appreciate the question. And we're working on a lot of levers at this point in time. And it was -- the three pillars is the one side of it. And as you can recall from what I've said, we're going beyond that. We're working on SG&A. We're looking at our structures.

We're looking at commercial excellence. We're looking at how effective our procurement is. We're going into our engineering structures. We're looking at engineering efficiency. And then to a certain extent, obviously, that might not be too strongly related to margin.

We're also looking at our innovation and how we're moving ahead there. And everything to an extent will have an effect on margin and will have a positive effect on margin. But I think it's now 100-plus days, so quite early. So give me some time while I work through all these levers and while I'm trying to improve all these levers for Sensata. And I'm sure we'll have more details and insight on that at a later stage.

Guy Hardwick - *Freedom Capital Markets - Analyst*

Okay, thank you. And just a quick one for Brian. Maybe I missed it cause I missed the start of the call, but are there any sort of financial issues from the ransomware attack you reported a month ago?

Brian Roberts - *Sensata Technologies Holding PLC - Chief Financial Officer, Executive Vice President*

No. You'll see in Stefan's prepared remarks, there was some obviously disruption to the business over the course of a couple of week period. That's all behind us now. The teams did a super job being able to work their way through it and get us back up and running. We don't expect it to have a material impact on the financial results for the quarter, so we're all systems go.

Operator

This concludes our question-and-answer session. I would like to turn the conference back over to Brian Roberts for any closing remarks.

Brian Roberts - *Sensata Technologies Holding PLC - Chief Financial Officer, Executive Vice President*

Thanks. Just want to thank everybody for joining today. Sorry that the call wound up a little later, but our normal cadence, part of that was just with the ransomware attack. I wanted to make sure we had appropriate time to get through our closing process. We'll get back to our normal schedule next quarter and look forward to updating you then again at that point. So take care, everybody. Thank you.

Operator

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

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