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IDEX Corp. (IEX)

Q1 2015 Earnings Call

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CORPORATE PARTICIPANTS

Michael J. Yates
Vice President and Chief Accounting Officer

Heath A. Mitts
Senior Vice President and Chief Financial Officer

Andrew K. Silvernail
Chairman and Chief Executive Officer

OTHER PARTICIPANTS

Matthew McConnell
RBC Capital Markets LLC

Joe K. Radigan
KeyBanc Capital Markets, Inc.

R. Scott Graham
Jefferies LLC

Mark Douglass
Longbow Research LLC

Brian Konigsberg
Vertical Research Partners LLC

Kevin R. Maczka
BB&T Capital Markets

Allison A. Poliniak-Cusic
Wells Fargo Securities LLC

Joseph C. Giordano
Cowen & Co. LLC

MANAGEMENT DISCUSSION SECTION

Operator: Greetings and welcome to the First Quarter 2015 IDEX Corporation Earnings Conference Call. At this time, all participants are in a listen-only mode. A brief question-and-answer session will follow the formal presentation. [Operator Instructions] As a reminder, this conference is being recorded.

It is now my pleasure to introduce to your host, Mr. Michael Yates, Vice President and Chief Accounting Officer for IDEX Corporation. Thank you, Mr. Yates. You may begin.

Michael J. Yates
Vice President and Chief Accounting Officer

Great. Thank you, Adam. Good morning, everyone. This is Michael Yates, Vice President and Chief Accounting Officer for IDEX Corporation. Thank you for joining us for our discussion of the IDEX first quarter financial highlights. Last night we issued a press release outlining our company's financial and operating performance for the three-month period ending March 31, 2015. The press release along with the presentation slides to be used during today's webcast can be accessed on our company's website at www.idexcorp.com.

Joining me today is Andy Silvernail, our Chairman and CEO; and Heath Mitts, our Chief Financial Officer.

The format for our call today is as follows: we will begin with Andy providing an update on what we are seeing in the world and then he will review the first quarter financial results; he will then walk you through the operating performance within each of our segments; and finally, we will wrap up with an outlook for the second quarter and the full year 2015. Following our prepared remarks, we'll then open the call for your questions.

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As we begin, a brief reminder. This call may contain certain forward-looking statements that are subject to the Safe Harbor language in today's press release and in IDEX's filings with the Securities and Exchange Commission.

With that, I'll now turn the call over to our Chairman and CEO, Andy Silvernail.

Andrew K. Silvernail

Chairman and Chief Executive Officer

Thanks, Mike. Hey, good morning, everybody. I appreciate you joining us here for our first quarter conference call in 2015. As we look at the first quarter, really the conversation has been dominated by some of the bigger issues that are floating around the macro environment; obviously, the strength of the dollar, the fall in oil prices and what I call a continuing overall slow economic environment. With those items as a backdrop, I'm very proud of the quarter that we just delivered.

We just delivered $0.84 in earnings with an op margin of 20.3%. We had 2% organic order growth and we built $22 million of backlog. We had organic sales and op margin improvement in Fluid & Metering and in Health & Science we had organic order growth and really outstanding profit execution and improving operating margin.

As you know, we foresaw a lot of the issues that we're all living with right now last year. We took very aggressive cost actions in the backend of the year and it certainly has prepared us for the environment that we're in and I think again our ability to get ahead of the curve with some challenging items.

We all know that we had these discrete comps that we're comparing against here this year with the dispensing in particular and the macro environment that I just mentioned. But we did see some I'd say some decline here in the overall environment as we moved through the second quarter and I'll talk about this in more detail in the segment review, but the combination of the agricultural market that's being slower, the increasing impact of the dollar, and while we've seen some slowdown in some large capital projects, are going to hit us by about $0.15 compared to what we talked about here in the first quarter, excuse me, the fourth quarter. And so we've revised our guidance to $3.50 to $3.60.

As always, we are very focused on controlling our own destiny. We can't control the overall macro environment and what you will see in this quarter and what you will see for the balance of the year is outstanding execution on the profit side with a real focus on our key products and our key customers. Our core business remains very solid and we are focused on delivering for our customers with real world-class execution. And so as I walk through the items here in the first quarter call, I will certainly highlight those pieces of that.

Before we get into the segment discussion, let me just talk about what we're seeing around the world and also around capital deployment. In North America, as I mentioned, the Ag markets and the energy markets, as we all know, have been soft. But that said, our daily book-and-turn business remains solid and we expect that to be so throughout the year. The one thing that I do think is a little bit different than when we talked to you here a quarter ago is that we have seen some slowdown on the capital side, capital spending, and we're keeping a pretty close eye on that. It's not widespread at this time. It's really focused around our Material Process business and in the energy facing markets, but we are certainly paying attention to it.

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Europe; Europe remains a tough slog generally, but we did see a modest pick up here, specifically in our businesses that touch the municipal markets and we saw that in China too, but we did see a slight uptick. I certainly wouldn't call it a sustained improvement, but we did see a modest uptick. China, as I mentioned a moment ago, the reported numbers that we all see, they really don't show themselves on the industrial side. With the exception of the municipal markets, which have improved, the China markets really remain consistent with what we've seen here for the last year or so.

And with that, let me turn to capital deployment. We have talked about a very balanced capital deployment plan with four pillars to our plan that remain unchanged. The first is we are always going to fully invest in organic growth and we've continued to make meaningful investments around our core products and our core customers. I'll touch on some of those as we move through the segment discussion. And we do think that will continue to allow us to differentiate over time and continue to really go after the most attractive profit pools in our markets and our customers.

You saw on April 8 we increased our dividend by 14% at $0.32 a share that we are committed to being in that 30% range. We're a little bit higher than we have historically been right now. But with our outstanding cash flows and our great balance sheet, we thought that was a prudent move. In terms of share repurchases, we would expect it will be net 2%, 3% this year as we move through the year. And in the first quarter, we repurchased 830,000 shares at a cost of $62 million.

The final pillar to our capital deployment plan is strategic M&A, and this continues to be a very important part of our overall capital deployment strategy and our business strategy. And you saw yesterday that we signed the agreement to acquire Novotema. We've been talking to Novotema for over a year, as a matter of fact, and we've looked at this business a couple of times over time. And we finally were able to get an agreement signed. We expect it will close in the neighborhood of 45 days pending regulatory approval.

This is an outstanding business. It fits squarely within our precision sealing platform. It marries the materials capability of PPE with some really outstanding manufacturing capability within Novotema. And as a matter of fact, we had been in partnership with them, touching a number of end markets before we agreed to acquire the business.

We're going to pay €57 million; it's about €30 million in sales, highly profitable. And after the impact of typical acquisition-related cost, it will be accretive out of the gate. Please keep in mind that our guidance for the balance of the year does not include any of the cost or the benefits of Novotema.

As you look at the rest of our M&A pipeline, it really is quite strong and I wouldn't say it's any change necessarily in the markets, but a lot of the hard work we've been doing here for a long time is coming forward. And as I talked about in the last call, we expect to spend north of $250 million this year and we remain committed to that bogey.

With that, let's move to slide four and we'll talk about the overall financial performance. Orders were $524 million. That was down 2%, but it was up 2% organically and we had improvement in all three segments. We had revenue of $502 million, which is down 8%, down 4% organically and we had op margins that were down 60 basis points at 20.3%.

Obviously, we've been talking for a long time about how the first quarter would shape up and the fact it was a very difficult comp. As you know, we had the majority of that large Dispensing order fulfilled in the first quarter of last year. And so that makes certainly for very difficult sales comps but also margin comps because as you'd imagine that flows through at a nice profit level.

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Cash flow for the quarter was $43 million. That was down $14 million from last year, but it really is impacted by principally a retirement – excuse me, a pension payment that typically falls in the second quarter and it happened to fall in the first quarter this year. So, on an operational basis very much in line with our expectations. And finally EPS for the quarter was $0.84 and that was down 8% compared to last year.

With that let's turn to the segment discussion. I'm on slide five, and I'll start with the Fluid & Metering. So FMT closed the quarter at a 1% increase in organic orders and a 1% increase in organic sales. They improved op margin by 30 basis points. Again, just really good execution across the board, and the impact of the restructuring actions that we took in the balance of last year.

The petrochemical and the chemical markets remained consistently strong in Europe and North America. We're optimistic throughout this year we see through our distribution and through the pipeline of business that that should remain a solid force through the balance of 2015.

In particular, Viking has just done a great job. The team at Viking in terms of sales, profit execution, customer intimacy, they've really been nailing it here for quite some time and did so again here in the first quarter.

Water Services, again, I mentioned the improvement in the municipal business really globally and we're seeing that in Water Services, but on a discrete basis, the ROVION system that we launched in our iPEK business has been a real winner for us. And a great example of our investments in organic growth, and they've taken nice chunks of market share and it really shows what you do when you focus on driving great products.

Energy; our midstream business is pretty good from a book-and-turn basis. It's really the large capital stuff that's closer to the wellhead that has been down really on a global basis, and that's going to be throughout the balance of this year. Not a surprise to us and that team is certainly managing their business for that new demand pattern.

Finally, Ag. I would say this is one place that did surprise us a little bit in the first quarter. We knew that the Ag market was soft. We have been preparing for that. But we did see even a more rapid decline in the OEM Ag business than we had expected. The overall distribution business in the industrial business remains good and I think it's important to remember that Banjo has just been a great performer for us for years. It's a terrific business, highly profitable, and they'll manage their way through what we all expected and certainly will turn at some point here. But it will be a challenge for the balance of the year.

With that, let's go to slide six on Health & Science. We had 2% organic order growth in the quarter. Organic sales were flat, but really just outstanding profit execution; up 150 basis points, improvements in productivity, great job of really going after the most attractive profit pools with new products and also the benefits of the restructuring that we went after last year. Scientific Fluidics, in particular, the analytical instrumentation market remains good and we expect it to be so for the balance of the year. They came into the year with a nice backlog and they go into the second quarter again in a nice position.

Optics & Photonics remain stable. Terrific profit execution. As we've talked about in the last quarter, this business is now from a profitability standpoint where we expected it to be and demand remains stable. Industrial, the book-and-turn business is good. So the more industrial-facing pieces of HST remains pretty good, and we expect it will be for the balance of the year.

The concerning spot for us is really Material Process Technologies. As you know, this is a longer cycle business, more exposed to capital projects and we did see a weak quarter in orders and sales, and given our visibility, we know how that will play out through the balance of the year in terms of overall sales and so we have a pretty good mark on where that will land for the year.

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Let's go to our last segment, that's Diversified, I'm on slide seven. So, organic orders were up 2% and as you all know, we expected substantial headwind on the sales front, which is down 16% organically, and of course that flows itself through as it impacts the margin from that large Dispensing order, so op margins were down 340 basis points, but down from a really incredible level last year, so we're still north of 25% in that business.

So we've talked a lot about the large Dispensing order; don't need to go through that again, but as you look past that, you see continuing really a strong business profile there. Europe has gotten better in the Dispensing business and the X-Smart product that we launched here a couple years ago continues to really be a juggernaut for us. It's been a great new product and like ROVION a great example of investing in core products for businesses, markets that we know well, and a great execution.

Fire Suppression, the North America and UK are solid; no indicators of softness there. China has been a little bit soft, but we are expecting that to pick up here as we look through the balance of the year with some of the improvement in municipal spending. Rescue, we've actually got some nice momentum. We've talked about last year really that being a soft spot for us and first time in a long time that that business had not seen the kind of robust growth that we were used to. We've seen some momentum here in the first quarter, and as we look in the pipeline, whether it's in North America, because of the success of eDRAULIC or some of the turnaround in the Asian markets, we're seeing some improvement there.

The concern, and this is a rarity for us, has been Band-It. Band-It is one of our businesses that has a decent exposure to oil and gas and they have been hit by that. Their industrial business, their kind of book-and-turn business remains good, but they have been impacted. And the one thing I certainly know about the Band-It business is they know how to perform regardless of the market and we expect them to turn that around as we move through the year.

All right. Let's go to slide eight and let's talk about guidance. As I stated before, we are revising our guidance for the year to $3.50 to $3.60, and I'm going to walk you through the discrete pieces of this and hopefully that will help you out here as you think about how we're considering the guidance.

The first is really the impact of the dollar. So, versus where we were in the fourth quarter call to where we are now, that's about a $0.06 headwind for us through the balance of the year. And in total is about $0.21 for the full year. So obviously from a top line standpoint, we thought that the change in the dollar was going to hit us by about $85 million and now it's going to hit us somewhere in the $110 million range at current FX rates. And that flows through at 20-ish percent plus or minus. It's mostly translational impact, it's all translational impact, but obviously that's a big headwind as we look through the balance of the year.

Ag; just given the very high profitability of Banjo and where that's playing out, that's going to hit us by about $0.04 incrementally through the balance of the year. And as we look at these large projects, whether its material process or some of the more energy facing that's about $0.05. And so, again in total it's about $0.15 compared to where we were at the fourth quarter.

All right. Let me go to the final slide here; slide nine. And let's reconcile the second quarter and some of the final items. So in the second quarter, we expect earnings of $0.88 to $0.90 and op margin of about 21%. That compares to $0.88 last year. Tax rate we expect to be about 29.5%, with again about 6% top line sales headwind from FX, which is about $0.06 just in the quarter versus last year.

Here's a couple of other items for you as you think about your modeling. I would expect op margin to be about 21% for the year. Top line, as I mentioned before, will be impacted by about $110 million versus $85 million that

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we talked about before, and again about $0.21 of EPS pressure. Full year CapEx still in the $45 million range. We expect free cash flow will be at that 120% that we talked about here at the end of the year. And we should repurchase in the neighborhood of 2% to 3% net shares here for the year.

As I mentioned before and as we always close out, this doesn't take into account any of the impact of acquisitions. And we will update you here on the second quarter call of all the impact of Novotema. There will be the classic step-up charges, et cetera, that we'll have and we'll net out all the impact for you as this plays on.

With that, Adam, I'm going to stop there and let's turn it over for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you very much. Ladies and gentlemen, we will now be conducting a question-and-answer session. [Operator Instructions] . Our first question comes from the line of Matt McConnell with RBC Capital Markets. Please go ahead with your question.

Matthew McConnell
RBC Capital Markets LLC

Q

Thank you. Good morning, guys.

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Hey, Matt.

Matthew McConnell
RBC Capital Markets LLC

Q

I am hoping you can provide a little more clarity on these large project headwinds. And it's sounds like midstream oil and gas is still kind of holding in pretty well but maybe correct me if I'm wrong there. So, is the uncertainty bleeding into other industrial markets or is this specific to upstream oil and gas or just maybe a better sense of what these large project headwinds are?

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Sure, sure. So, yes, you're correct, Matt. The midstream has held in nicely and we expect that will for the balance of the year. The real issue is really the oil and gas side and again that's kind of in line with our expectations. I will say that the capital freeze – and we expected it to be pretty aggressive – the capital freeze that we're seeing in the U.S. in particular has been pretty significant, so that's one area. The other area has been around material process, and that's more general industrial facing. A pretty decent amount of that is touching in the world of foods. And so we have seen that hold up a little bit.

We have not seen, what I'll call, broad-based capital freeze, but whenever you see some of this start to move like this, it raises the red flag. And so we're paying an awful lot of attention to it. We have all of our businesses paying a lot of attention to it. Historically, we have been able to see slowdowns coming and I wouldn't necessarily say that we're there. I don't want you to get that message at all. I just want you to get the message that we've seen a couple places where it's slowed down and we want to make sure that we've got our antennae up.

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Matthew McConnell
RBC Capital Markets LLC

Q

Okay, great. Yes. That makes sense. I mean orders weren't even down in any of the segments. So, it certainly seems like you are staying in front of it. So, then on profitability of Novotema, anything you can help us with there. I know you gave us the multiple on sales. Anything on EBITDA?

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Yes. So, it's very profitable business. From an EBITDA margin, it's IDEX like. It's not going to be dilutive to our margin. Matter of fact, it's going to be accretive overall from an EBITDA perspective. It's a very, very profitable business and the team there – we've known this business for a long time, and they've done a great job of repositioning that business over time to be in more attractive markets and it's really a wonderful combination between PPE.

So, if you remember, and we bought PPE back in 2010, and there are a few things that are really unique about PPE. One of them is they have some really unique capability in material sciences. And so as we were looking at Novotema, the question we had is given Novotema's strengths in certain end markets and in manufacturing capability, could we marry their great manufacturing and some of their end markets with our material science capability and have the same kind of very quick turnaround for customers, whether it's new product development of operationally, could we do that? And the answer to that is yes.

And so, we actually – before we decided to move forward with the acquisition, we actually partnered with them and to see if we could do this on a commercial basis. So, we actually created a commercial partnership around our material science capability, their manufacturing capability and it really was incredibly successful and convinced both parties that this was the right marriage. And so we're excited to have them part of the family.

Matthew McConnell
RBC Capital Markets LLC

Q

Great. I appreciate that insight. Thank you.

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Thank you.

Operator: Thank you. Our next question comes from the line of Scott Graham with Jefferies. Please go ahead with your question.

R. Scott Graham
Jefferies LLC

Q

Hey, good morning.

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Hi, Scott.

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R. Scott Graham
Jefferies LLC

Q

So, in the interest of getting Heath to say something...

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

We have no [ph] chance of that (24:00) here.

R. Scott Graham
Jefferies LLC

Q

My hope is that maybe you guys – and it's really my only question because I thought your presentation was very clear and everything made sense. Typically you go for a certain level of productivity each year. So what do you now need incrementally to that dollar wise? Is it $10 million? Can you just size that number for us to offset the sales shortfall?

Heath A. Mitts
Senior Vice President and Chief Financial Officer

A

Well, Scott, thanks for giving my time in the sun here. We're off to a really good start from a productivity perspective this year and I think that's reflected in the margins. You see it; our ability to counteract. Going into the quarter, we knew we were going to have the headwind year-over-year from the large projects within Dispensing, but our ability to more than offset that and as well as the FX pressure is reflective in the segment operating results and we're very pleased. I wouldn't say pleasantly surprised but very pleased with their performance there.

We've talked in the past about going into any given year with roughly a $25 million headwinds in terms of inflation. Certainly the material inflation is something that we're able to hold down a little bit this year in this environment, but the wage inflation is still real, which is the 60% or so of that $25 million. So, given all that, we are on track to counteract what our normal productivity, both sourcing savings as well as OpEx type of savings around scrap and overtime reduction and the ability to lever our fixed cost base is still well on track.

Now, in terms of an incremental downtick relative to when we started the year, as you know we did a fair amount of restructuring savings in the fourth quarter where we ended up taking out about $15 million or $16 million of annualized cost. That certainly has provided some level of protection and we will consider any additional actions as necessary as we progress through the year, albeit it's going to be somewhat selective in terms of where and how we would do those things. We don't want to cut too close to the bone in any one area because we are making strategic organic investments and we don't want to lose that momentum.

R. Scott Graham
Jefferies LLC

Q

Understood. So essentially the answer is you're on track with productivity to offset your normal inflation and the incremental this year is still in the restructuring savings, but if necessary there might be a little bit of upside to that if sales don't necessarily come through. Is that a fair paraphrase?

Heath A. Mitts
Senior Vice President and Chief Financial Officer

A

You summarized it well.

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R. Scott Graham
Jefferies LLC

Q

All right.

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Scott, this is Andy. If you kind of dimentionalize all this together, I don't think we've talked about it like this necessarily, but when you look at FX, you take FX, you take the impact of the large businesses that – or comps from last year, those two things together, you're talking about $35 million of profitability together that we're comping against, plus the normal $20 million to $25 million of just inflation. So you're talking about in the neighborhood of $50 million to $60 million of profit comp that we are going to cover, right, as we go through this year. So even with the guidance that we have as we sit here today, sometimes we lose sight of the magnitude of the execution that the teams have done and it's damn good.

R. Scott Graham
Jefferies LLC

Q

Appreciate it, but in continuing to answer my question, Andy, I came up with another question.

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Okay.

R. Scott Graham
Jefferies LLC

Q

I hope you don't mind.

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

[indiscernible] (27:57).

R. Scott Graham
Jefferies LLC

Q

It just kind of hit me, you were talking about the puts and takes and as you're weaving that together, how is the pricing component of things right now?

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

It's actually – it's holding up, right. It's I would say total pricing is a little softer than we saw last year, meaning we're not getting quite as much, but you're still talking about call it the 1% range that we're going to get. We've gotten a lot of questions about are we seeing price in oil and gas and we're fortunate given where we play in the food chain that we're not seeing that. I mean, heck, everybody gets the letter that says, hey, we want a price reduction, but given our proprietary positions, whether it's technology or the switching costs, we're able to hold up prices pretty well.

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R. Scott Graham
Jefferies LLC

Q

Very good. Thanks, guys.

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Thank you.

Operator: Thank you. Our next question comes from the line of Brian Konigsberg with Vertical Research Partners. Please go ahead with your question.

Brian Konigsberg
Vertical Research Partners LLC

Q

Yes. Thank you. Good morning.

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Hey, Brian.

Brian Konigsberg
Vertical Research Partners LLC

Q

One of my two questions were taken, but I will go on to the question not asked about. So just on FX, can you just talk about how that may be impacting you from a competitive standpoint? Is it becoming more difficult to compete against some of the European players, particularly maybe in HST or maybe if there is other areas in the portfolio that might have that type of dynamic going on?

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

So, there are puts and takes relative to that, competitively. So we're pretty fortunate that the vast majority of what we do kind of where – we manufacture where we compete typically. And so we don't necessarily see that competition. Although you certainly will see some overseas competition in European competitors trying to go after, say, the U.S. market where we have a strong foothold. This is just – and I'm just using an example. So you will see some of that, but this is again I've used the term, these markets are glacial, and for good and for ill the markets move really slowly.

And so I think the question that you're asking is more of a if we stay in this sustained area for a few years, will we start to see it on new business that's playing through, right? So, so much of our business is going into an aftermarket or a like-for-like replacement versus kind of large contracts that are going out. And so it would take years to kind of play through from a competitive standpoint. So that's one thing. So we're not seeing it today.

The other part is, remember we've got a pretty decent footprint in other parts of the world. 50% of our business is non-U.S. and 40% of it is actually produced outside of the U.S. So while we may see some things in a few years if the current currencies play themselves out, we also have the benefits of being more competitive in the businesses that we have outside of the U.S. So I don't expect it's going to be a big impact that we'll see.

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Brian Konigsberg
Vertical Research Partners LLC

Q

Great. And maybe just to follow-on, on the Water business, clearly you're doing very well gaining share, bringing new products to market. The underlying market itself there, are you starting to see things starting to firm up? We know a number of projects have been delayed over the last couple years. Are those starting to break loose or is really your success here just a matter of market share gains?

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

I would say we are seeing the improvement. I would say the number of municipal bids that are going out and in particular the number of large dollar bids that I think people were really hesitant on in North America in particular have improved. And so, if you recall, we made a real conscious decision to reposition ourselves relative to the markets that we were going after in Water Services in the U.S. and in the UK. And that was the right move => in terms of focus and going after the right profit pools then. And I think it's going to pay dividends for us as those places start to free up a little bit more capital. So the businesses are better in the U.S. and in Europe, and we should say the UK. I should say in North America and the UK and also in China we've seen that a little bit. So we've seen some level of improvement in China.

Brian Konigsberg
Vertical Research Partners LLC

Q

Great, I'll pass it along. Thank you.

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Thank you.

Operator: Thank you. Our next question comes from the line of Allison Poliniak with Wells Fargo Advisors. Please go ahead with your question.

Allison A. Poliniak-Cusic
Wells Fargo Securities LLC

Q

Hi, guys. Good morning.

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Hi, Allison.

Allison A. Poliniak-Cusic
Wells Fargo Securities LLC

Q

Hi. Just, Andy, on the organic investment side, obviously, your use of cash, can you maybe talk about how you're looking at it I guess maybe in this uncertain environment? I know some of your markets are bigger and harder to move, but is there a share gain opportunity for you? Are you becoming more selective because of certain end markets at this point?

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Andrew K. Silvernail
Chairman and Chief Executive Officer
A

Yes. You have to think about organic investments at IDEX in a multi-year phase or thought process. And the reason I say that is, if you think about generally any business that we have from the time of concept through I'll call it full demand, you are talking about a five-year timeframe if you're realistic about it. And so the things that we're winning on now, if you go back to 2012 when we talked about making some major choices and cutting and building in 2012, the benefits that we're seeing today with those investments then. And I know sometimes for the investment community that can be unfulfilling because you don't get the rapid speed that you get, but that's also why the markets are so darn defensible. And so the investments that we're making today, in reality they're not going to show up for two, three, four, five years in full, but we know that we've got to have the patience and the discipline to play that out.

The Diversified space in general gets a lot of criticism around organic growth and I've been asked many times what's underneath that, and my belief is frankly we don't have the discipline and the patience to make the multi-year investments and you have do it and that's what we've done.

Allison A. Poliniak-Cusic
Wells Fargo Securities LLC
Q

That's great. And then last call you talked a little bit about energy and maybe potential benefit as we move to the end of 2015 into 2016 from the sort of energy tax relief we're getting here. Any thoughts on that? Updates, changes from that there?

Andrew K. Silvernail
Chairman and Chief Executive Officer
A

It's not playing itself through yet, except maybe the one place that we're seeing it is actually in Dispensing. And the reason I say that is demand that's going through the retailers, which is putting more money in their pockets. And so if you look at the Dispensing business, really on a global basis that's been pretty good, right. So if you look at the overall business there as capital is flowing through those retailers and allows them to refurbish, it is allowing for that to flow through dispensing to some degree, it's hard to peg it exactly Allison, but I would say it's one place that you could draw a line to. How it plays through the general economy and that was my statement at the fourth quarter call, typically that can be a year or more before it goes to the consumer into the business community. So, I still think, we are going to live with that gap where you've seen massive capital cuts in the energy world. And of course, now we're seeing the daily layoffs that are happening in those places. You're going to see that be the near-term impact and then maybe at the end of this year in 2016 you'll see how that flows through back to the business community.

Allison A. Poliniak-Cusic
Wells Fargo Securities LLC
Q

Perfect. Thanks guys.

Andrew K. Silvernail
Chairman and Chief Executive Officer
A

Thank you.

Operator: Thank you. Our next question comes from the line of Joe Radigan with KeyBanc Capital Markets. Please go ahead with your question.

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Joe K. Radigan
KeyBanc Capital Markets, Inc.

Q

Thanks. Good morning, guys.

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Good morning, Joe.

Joe K. Radigan
KeyBanc Capital Markets, Inc.

Q

I guess, first what percentage of MPT is driven by project activity? And then maybe the same question for the energy piece of FMT?

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

So for MPT it's going to be in that, call it, 40% range plus or minus that has a larger capital piece to it. And when I say larger capital, let's dimensionalize that, you're talking about $250,000 to sometimes a several million dollar project, but those are pretty rare. So when we say large capital, we're not talking about $50 million projects or anything like that. But you can see it certainly in a quarter or two that are dry or robust. You can see how that's going to play itself through really for the balance of the year. So the order softness that we saw here in the first quarter, that's going to play itself through as we get to the third quarter and the fourth quarter in particular, second quarter is actually okay in terms of what we can see in the funnel. So that's a little bit more lumpy than we're used to seeing within IDEX, but that's kind of the dimensions we're talking about.

Joe K. Radigan
KeyBanc Capital Markets, Inc.

Q

Okay. And then Andy, I'm sorry...

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

We don't have the same magnitude in the energy side.

Joe K. Radigan
KeyBanc Capital Markets, Inc.

Q

Okay. And then just to be clear, have you seen any orders that were already in backlog get cancelled or is this more restricted to kind of the go-forward order rates?

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

It's really around go-forward. Again, generally, we don't have a lot of exposure to kind of big capital stuff that's in the pipeline that we have committed and we have an order getting cancelled. When we see a large capital project, let's just say in energy, we have some business that may go into it, let's call it in that $250,000 to $1 million range, but more of it is understanding kind of how that pipeline is going to flow to what we call our book-in-term business.

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And so, you'll see BAND-IT as an example. Well, when you know a large capital project is happening, we know we're going to get a large chunk of that business, but it's not committed until kind of really late in the process. So we don't have a lot of things sitting on our books today that are at risk of being cancelled, it's more of kind of understanding what that pipeline is going to look like here over the next 6 months to 12 months.

Joe K. Radigan
KeyBanc Capital Markets, Inc.

Q

Okay. And then I guess my next question actually is around BAND-IT. And again, you've talked about that being sort of a bellwether for the overall economy since it touches so many end markets....

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Yeah.

Joe K. Radigan
KeyBanc Capital Markets, Inc.

Q

... and it's short cycle. If you exclude the oil and gas piece of it which is understandable, have you seen any trends kind of in that base run rate business that either give you cause for concern or vice-versa, reason for encouragement?

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

That's a great question, because as we were looking at their order rates and as we go through our typical business reviews, we asked kind of that same question. So we actually asked them to look specifically at – we have in energy vertical within BAND-IT, so we could kind of see that piece. But then we saw some weakness that we were like, wait a second here, what's going on? So we asked them to kind of dice up the country and look at it. And lo and behold, all of the weakness that they found happened to be in the four states that have enormous energy exposure, so really isolated to energy, the normal kind of general distribution book-in-term business, transportation business is quite good.

Joe K. Radigan
KeyBanc Capital Markets, Inc.

Q

Okay. And then maybe one more question on HST. How should we think about the organic growth for the balance of the year? You have a relatively easy comp in the second quarter, but then...

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Yeah.

Joe K. Radigan
KeyBanc Capital Markets, Inc.

Q

...you are facing plus mid-single-digits in the back half, book-to-bill was good, but orders were only up organically 2%. So how are you thinking about the trajectory in HST?

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

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I think we're going to be looking at kind of 3% to 4%...

Joe K. Radigan
KeyBanc Capital Markets, Inc.
Q

Okay.

Andrew K. Silvernail
Chairman and Chief Executive Officer
A

...3% to 4% organically. But let me kind of parse that a little, because I think that's important. I think what you'll see are meaningfully stronger numbers in Scientific Fluidics, I think you'll see that the strength there in Optics and you'll see the weakness that we just talked about a moment ago in MPT as it plays through the third quarter and the fourth quarter. So as you think about kind of the core markets that we really spend a lot of time on and we've put a lot of our core investment in, we think that's going to be actually pretty decent here as we move through the year.

Joe K. Radigan
KeyBanc Capital Markets, Inc.
Q

Great, thanks a lot Andy.

Andrew K. Silvernail
Chairman and Chief Executive Officer
A

Thank you.

Operator: Thank you. Our next question comes from the line of Mark Douglass with Longbow Research. Please go ahead with your question.

Mark Douglass
Longbow Research LLC
Q

Hi good morning, gentlemen.

Andrew K. Silvernail
Chairman and Chief Executive Officer
A

Hi Mark.

Mark Douglass
Longbow Research LLC
Q

That leads me into looking at FSD, the Dispensing order comp, what do you expect for 2015, the Dispensing order comp was about $20 million in 1Q 2014 is that about right?

Andrew K. Silvernail
Chairman and Chief Executive Officer
A

You are talking the sales number?

Mark Douglass
Longbow Research LLC
Q

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Yeah sales number.

Andrew K. Silvernail
Chairman and Chief Executive Officer
A

Yeah it was more like $24 million.

Mark Douglass
Longbow Research LLC
Q

$24 million.

Andrew K. Silvernail
Chairman and Chief Executive Officer
A

It was a big number.

Mark Douglass
Longbow Research LLC
Q

Okay. Because initially I think some of it you thought would roll into second quarter, and...

Andrew K. Silvernail
Chairman and Chief Executive Officer
A

Yeah. If you recall the first quarter last year we ended up having a really strong first quarter, principally because we did pull – our customer assets to pull it forward into the first quarter.

Heath A. Mitts
Senior Vice President and Chief Financial Officer
A

Hey, Mark, this is Heath. Just to clarify though, what we talked about earlier in the year was about a $50 million worth of big projects. There was a very specific – that's made up of two specific Dispensing orders and one in the Fire Suppression space. So, in the first quarter, it was about half of that $50 million.

Mark Douglass
Longbow Research LLC
Q

Right.

Heath A. Mitts
Senior Vice President and Chief Financial Officer
A

In the second quarter, it's the blended of the other two. So, in total, Dispensing is about $35 million made up of two projects and then there's about $15 million out of the Fire Suppression space. And so, we'll still have about a $20 million to $25 million headwind in Q2.

Mark Douglass
Longbow Research LLC
Q

Right. 3Q was pretty strong too.

Heath A. Mitts
Senior Vice President and Chief Financial Officer
A

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It was, but what we've talked about in prior year – or within our guidance is really the Q1, Q2 impact on the headwind. We did have a good Q3 last year, but it wasn't so much tied to very specific project activity.

Mark Douglass
Longbow Research LLC

Q

Okay, that was broader. Okay. So then my question and looking at 2015, I mean we're probably talking mid-single-digit decline organically?

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Yeah.

Heath A. Mitts
Senior Vice President and Chief Financial Officer

A

Low-to-mid.

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Yeah, low-to-mid, yep.

Mark Douglass
Longbow Research LLC

Q

Low-to-mid decline. Okay. In FMT, I believe you said, you were thinking low-to-mid single-digit growth, are we closer to flat to low single digits?

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

You're still talking up kind of 2% to 3%.

Mark Douglass
Longbow Research LLC

Q

2%, 3%?

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Yep.

Mark Douglass
Longbow Research LLC

Q

Okay, that's helpful. Thank you.

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Thanks.

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Operator: Our next question comes from the line of Kevin Maczka from BBT (sic) [BB&T] Capital Markets. Please go ahead with your question.

Kevin R. Maczka
BB&T Capital Markets

Q

Thanks, good morning.

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Good morning, Kevin.

Kevin R. Maczka
BB&T Capital Markets

Q

Andy, I just wanted to piggyback on the organic growth question, and I appreciate your commentary on the fact that you have to a take a long-term view and make investments now that that won't pay dividends for a few years. But can you just touch on why is that such a long cycle, why is it five years? Is it because in some cases you're almost inventing new markets and you have to prove to customers that they need that type of product? Or is it that you're trying to displace an entrenched competitor, and maybe that's not an easy thing to do?

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Yeah. So if you kind of break that, let's just use five years as – five years is when you're at, I'll call it kind of full volume so to speak. So you are talking a year or two that is going to be product development that's really when you're going from idea to having a product that you are able to launch into the marketplace. The industrial customers generally – unless it's – if it's just a basic revision of a product, that's a different story, but when you are talking a new product, these customers are very, very cautious. And so, you generally have testing that's going to happen and let's just call that a year plus or minus that you are going to see where people are really testing the solution.

And then you have the issue of just opportunity for uptake. And let me just give you an example of that. If you take a normal process facility and this is just a kind of way to think of it. Unless it's a new facility, they generally only have wash-up somewhere between two weeks or four weeks a year, so kind of maintenance shutdown. And so the opportunity for really bringing a product into an existing facility is there are relatively small windows, so you're then relying on some kind of refurb within a facility or you are looking at new facilities coming in online. So, when you blend that all-in, that's why that timeframe is as long as it is.

And, again, I said this before, while it certainly leads to some frustration around your ability to change the organic growth curve quickly, it's also the beauty of the defensibility of businesses like IDEX.

Kevin R. Maczka
BB&T Capital Markets

Q

Got it, that's helpful. And then, in FSD, you're calling the X-Smart product the juggernaut now, I don't think....

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

It's been great.

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Kevin R. Maczka
BB&T Capital Markets

Q

Yeah. I don't think there's too many individual huge needle movers within the IDEX portfolio. But to the extent you can talk about anything coming that we ought to be keeping an eye out for, is there something that you're particularly excited about here for the next couple of years?

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

That's a relatively unusual example for us. And, to give you a sense of it, that's going to be a $20 million product for us, when it's all said and done.

Heath A. Mitts
Senior Vice President and Chief Financial Officer

A

But, it's taken three or four...

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

But, it has taken three years, four years. I would put eDRAULIC into that same kind of category. And, in both those cases, what you solved for was really a gap in the market. And so, with X-Smart in particular, what you have now is you have an automatic dispenser that is really displacing an entire segment of the market that was manual dispensers, right.

So, you've got to the kind of price point that was attractive in specifically in the emerging markets that very much wanted the quality and the capability of an automatic dispenser. But they were never going to reach that price point that the western world could, where there is enormous volume and it makes sense to have that kind of product. So, we really solved that.

We've got a couple at Viking that are going to be in that $10 million range, one that actually will be in that $10 million range this year and a couple of other that are coming through the pipeline, that look that way. Certainly, within Scientific Fluidics, we have brought together – actually I'd say the combination of Scientific Fluidics and Optics, that promise of the idea of the optical fluidic engine, you've seen some promise in there, the marrying of fluidics and optics that has reached that kind of level, that $10 million to $20 million level. But for the most part, you are really talking about $5 million to $10 million chunks that we look at.

Kevin R. Maczka
BB&T Capital Markets

Q

Got it. Thanks again.

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Thank you.

Operator: Thank you. Our next question comes from the line of Joe Giordano with Cowen Group Inc. Please go ahead with your question.

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Joseph C. Giordano
Cowen & Co. LLC

Q

Hi, guys. Thanks for taking my question. I just wanted to touch on HST a bit here. So, you're growing mid-single digits back half of last year, now, flat organic. Am I right in thinking that that's almost entirely from MPT, like has there been a second derivative decline in fluidics or anything like that?

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

No, no. It's all MPT related.

Joseph C. Giordano
Cowen & Co. LLC

Q

Okay. And then quickly on muni, can you may be parse out the environments on break and fixed versus capital, I know you touched on it earlier with some of the larger projects and maybe U.S. versus Europe in those kind of splits?

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

So, the break fix business had been the stronger part. We did see a couple of things break our way in the U.S. here over the last couple of quarters and we saw a couple of big new installations or new projects rather in the U.S., I should say North America because we had one that was meaningful in Canada. And then, the UK, the [ph] EMP (49:00) cycles that you see over there, we have one, so major pieces of that and that showed up in our order rates and that will be a nice piece of business for us here over the next couple of years.

Joseph C. Giordano
Cowen & Co. LLC

Q

Great. Thanks, guys.

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Yep.

Operator: Thank you. Our next question is a follow-up from the line of Matt McConnell at RBC Capital Markets. Please go ahead with your follow-up.

Matthew McConnell
RBC Capital Markets LLC

Q

Thanks, guys. Just wanted to touch on Ag real quick.

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Yeah.

Matthew McConnell
RBC Capital Markets LLC

Q

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Based on its size, and I guess the aftermarket content, I'm surprised it even has the capacity to drive a measurable change to the guidance growth. Are there any inventory adjustments in the channel or are you seeing aftermarket slow down a lot more than you expected, I would imagine that's usually fairly steady? But just maybe size the aftermarket content there, and whether that's also participating in this weakness?

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Sure, sure. Well, first thing to keep in mind is, this is a very high contribution margin business. So certainly, as you look on the continuum of IDEX, this is on the far side from an overall contribution margin. And so a small top-line hit is meaningful on a bottom line, just because it is at the level it is and there just isn't the cost structure to rip out so to speak, nor would you want to in a business like that that you believe long-term in there. So relative to the demand side Matt, the OEM side is sharper than we would have expected. And I will say that in the Ag distribution channel, there is a lot of inventory, there is no doubt about it. And so that's going to play itself through.

In terms of the aftermarket, meaning again kind of the break fix stuff, that's going to hold up well, right. Because at the end of the day, if you're running a sprayer as an example, you've got to do the maintenance on it this year. And typically, what we see happen in cycles like this is, people aren't buying new equipment. And so, they are not retiring the old equipment – well they are retiring the old equipment and what you see now is the older equipment having a little bit longer lifecycle.

And so, that would be better, but the amount of new product in the channels and what's happening in the OEMs in terms of their production schedules, that's pretty significant. And farm prices or farm profits have been hit, and you guys all know the story here better than anybody. The farm profits have been hit meaningful and that's going to take at least this year to play through, and we'll kind of judge the impact on next year.

Matthew McConnell
RBC Capital Markets LLC

Q

Okay. Great. Thanks very much. That helps.

Andrew K. Silvernail
Chairman and Chief Executive Officer

A

Thank you.

Operator: Thank you. Ladies and gentlemen, we have no further questions at this time. I would like to turn the floor back over to the management for closing remarks.

Andrew K. Silvernail
Chairman and Chief Executive Officer

Well, thank you, Adam. And again, we appreciate your interest in IDEX and the ability to walk you through here what's going on. Obviously, we're very proud of the execution that we've been able to do here in the first quarter, but we recognize the realities of the world. And so, that idea of controlling your own destiny is something that we put front and center, and we're absolutely going to do so. We always keep in mind the long-term value creation for our shareholders and our desire to be one of the superior creators of value, and we're going to continue to work for you.

And so, we appreciate your support and we will talk to you here in 90 days. Thank you. Take care.

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Operator: Thank you again, ladies and gentlemen. This does conclude our teleconference for today. You may now disconnect your lines at this time. Thank you for your participation and have a wonderful day.

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