26-Oct-2022

IDEX Corp. (IEX)

Q3 2022 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Greetings and welcome to IDEX Corporation's Third Quarter 2022 Earnings Conference Call. At this time, all participants are in a listen-only mode. A 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 your host, Allison Lausas, Vice President and Chief Accounting Officer. Thank you. You may begin.

Allison S. Lausas

Chief Accounting Officer & Vice President, IDEX Corp.

Good morning, everyone. This is Allison Lausas, Vice President and Chief Accounting Officer for IDEX Corporation. Thank you for joining us for a discussion of the IDEX third quarter 2022 financial highlights. Last night, we issued a press release outlining our company's financial and operating performance for the three months ending September 30, 2022. The press release along with the presentation slides to be used during today's webcast can be accessed on our company website at idexcorp.com. Joining me today are Eric Ashleman, our Chief Executive Officer and President; and Bill Grogan, our Chief Financial Officer.

Today, we'll begin with Eric providing an overview on the state of IDEX's business. Then Bill will discuss IDEX third quarter financial results, provide an update on segment performance and the markets they serve and discuss our outlook for the fourth quarter and full year 2022.

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Following our prepared remarks, we will open the call for your questions. If you should need to exit the call for any reason, you may access a complete replay beginning approximately two hours after the call concludes by dialing the toll-free number, 877-660-6853 and entering conference ID 13724804 (sic) [ID 13724805] (01:50) or simply log on to our company homepage for the webcast replay.

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

With that, I'll now turn this call over to our CEO and President, Eric Ashleman.

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Thank you, Allison, and good morning, everyone. I'm on slide 6. Our global teams achieved excellent results in the third quarter. We delivered record sales, adjusted EPS and free cash flow. Organic sales grew 15% with double-digit record growth across all three of our segments.

Orders moderated a bit in the quarter, but backlog positions remained robust overall. It's been a strong record-setting year so far for IDEX, not easy to achieve in this environment. I'd like to thank all our IDEX employees around the globe for their outstanding efforts.

On the capital deployment side, last month, we announced our intent to acquire the Muon Group for €700 million, marking our largest acquisition to date. Muon expands upon a growing core of market-leading precision components technologies, an area of the portfolio we continue to invest in both organically and inorganically.

Muon's technical capabilities, like many others within IDEX, are well positioned, differentiated and tunable towards high growth niche applications within broader megatrends. Muon technologies solve critical problems within the most demanding application sets of semi-manufacturing, patient care within medtech, food production and other high quality markets. This acquisition demonstrates the success of our expanded M&A strategy. We combine bottoms up business intelligence with analysis and insights from a small strategic community across IDEX to build conviction within a grid of high quality niche applications.

Increasingly, as we build and optimize the portfolio, we find that we can drive growth within a target vertical from multiple points, organically from within IDEX businesses and externally via M&A. We think this approach is unique and advantaged. It leverages 80/20 and segmentation, our operating model and the quality and strength of our diverse collection of businesses.

We also completed the sale of our Knight LLC business in the third quarter. Knight supports cleaning and sanitization within hospitality and janitorial markets. As we discussed in the past, we continually seek to optimize our portfolio. When we identify businesses or product lines that would grow and thrive for other owners, we've divested those assets. I want to express my appreciation to the Knight team for all they've contributed in their 25 years with IDEX.

Next, I want to share some exciting organizational news. I'm happy to announce that Melissa Aquino recently joined IDEX as Senior Vice President, Group Executive for FMT and FSD. Melissa has a broad understanding of what it takes to grow and succeed as a team in manufacturing, having served in a wide variety of commercial, operational and leadership roles. She has scale and depth of experience across multiple industries, including

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consumer, industrial, diagnostic, and life sciences. Although we are aligning these segments under a single leader internally, they will continue to be separate reportable segments.

I'd also like to take a moment to celebrate the tenure and accomplishments of our HST Group Executive, Marc Uleman. We've seen outstanding results under his more than 10 years of leadership at IDEX driving organic growth, operational excellence and capital deployment in our fastest growing segment.

Finally, we recognize there's considerable churn in the global economy right now, whether tied to geopolitical uncertainty, inflation, interest rates or the fear of a recession. There are several scenarios that could play out, ranging from continued industrial growth to a shallow short-term pullback to a deeper recession. We have a plan of attack for each and I'm confident we'll outperform as we have in the past.

Our teams are smart and agile. They'll quickly adjust and put their best resources on the best opportunities. That's at the core of our operating approach. We've made great progress in building a strong and sustainable growth engine. It sits on top of a solid foundation of execution within any environment. That's the and not or that we talk about all the time at IDEX. We're leaning in as a team towards the challenges and opportunities ahead.

With that, let me turn it over to Bill to discuss our financial results.

William K. Grogan

Senior Vice President & Chief Financial Officer, IDEX Corp.

Thanks, Eric. I'll start with our consolidated financial results on slide 8. Q3 orders of 781 million were up 1% overall and down 1% organically. We experienced orders growth in FMT but some contraction in HST and FSD, primarily driven by timing of some larger orders. Core demand rates remained positive across the segments. Third quarter sales of $824 million were up 16% overall and up 15% organically. We experienced record sales with double-digit organic increases across all three of our segments and strong performance across all geographies.

Third quarter gross margin expanded by 250 basis points and adjusted gross margin expanded by 10 basis points compared to the prior year at 45.1%, driven by strong volume leverage and favorable price/cost, partially offset by higher employee-related costs. Third quarter operating margin was 24.5%, up 190 basis points compared to the prior year. Adjusted operating margin was 24.9%, up 60 basis points. Incremental amortization related to the Nexsight and KZValve acquisitions unfavorably impacted adjusted operating margin by 30 basis points. I will discuss additional drivers of adjusted operating income on the next slide.

Our Q3 effective tax rate was 21.8%, a decrease compared to the prior ETR of 23.4%, primarily driven due to the tax benefits associated with the sale of the Knight business. Third quarter net income was $179 million, which resulted in an EPS of $2.36. Adjusted net income was $162 million, resulting in an EPS – an adjusted EPS of $2.14, up $0.35 or 20% over prior year.

Finally, free cash flow for the quarter was $182 million, 112% of adjusted net income. This was a record free cash flow for us, mainly driven by higher earnings. We are seeing inventory levels stabilize and expect further reductions as we exit the year.

Moving on to slide 9, which details the drivers of our adjusted operating income. Third quarter adjusted operating income increased $28 million compared to last year. Our 15% organic growth contributed approximately $26 million flowing through at our prior year adjusted gross margin rate. We levered well on the volume increase, and we had strong price capture to offset inflation headwinds. Price/cost was accretive to margins and has returned to

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historic levels, driven by our FMT and HST segments, with FSD making improvements sequentially versus the second quarter.

We experienced slight positive mix of $2 million in various parts of the portfolio. We reinvested $6 million, taking the form of engineering and commercial resources into businesses, and M&A and DE&I resources at corporate, tracking to the $0.20 to $0.25 of full year spend we highlighted at the beginning of the year.

Lastly, discretionary spending increased by $6 million versus last year, which is slightly below the second quarter of 2022. As we said last quarter, we have reached a more normalized post-COVID spend rate on significantly higher sales volume. This delivered a strong organic flow through of 31% in the quarter. Flow through was then negatively impacted by the dilutive impact of acquisitions, divestitures and FX getting us to a reported flow through of 30%. With that, I'll provide a deeper look at our segment performance.

I'm on page 10. In our Fluid & Metering Technologies segment, we experienced excellent order and sales performance with organic growth of 2% and 17%, respectively. FMT adjusted operating margin expanded by 250 basis points versus last year. The increase included 80 basis points of headwind due to the incremental amortization related to the Nexsight and KZValve acquisitions. We experienced continued strong volume leverage and operational productivity as well as favorable price/cost.

Our industrial markets continue to exhibit steady demand with tailwinds from energy, mining and infrastructure tempered a bit by some European softness. Our outlook for our municipal water businesses continues to be positive. We see healthy quoting activities in sync with underlying market trends of growing urbanization, further CCTV inspection adoption and infrastructure investments in the US.

Agriculture remains strong. We are seeing positive signals from both our OEMs and distributors. Commodity prices remain high and increased fuel and fertilizer costs are incenting farmers to invest in precision technologies. Our investment in Banjo's process automation have improved our delivery, putting us in a good position to capture share. And we continue to leverage KZValve's expertise and technology to enhance our product offerings.

Our energy business is performing well with strong oil and LPG price support. We continue to see favorable results upstream with midstream investments lagging a bit due to supply chain constraints at our customers and larger project spend delays.

Moving on to the Health & Technology segment (sic) [Health & Science Technologies segment] (11:44), orders contracted by 4%, but sales were strong at 13%. Our backlog position remains robust. The contraction in orders was driven by several large orders that delayed out of the quarter. European capital goods softness and tough comparables from the prior year where we grew orders organically by 44%. HST adjusted operating margin contracted by 70 basis points versus last year. The segment experienced strong volume leverage and positive price/cost, which was more than offset by increased engineering and resource investments, higher discretionary spending and some inefficiencies incurred as we continue to onboard labor to meet demand and navigate supply chain challenges.

We continue to experience strong demand for analytical instrumentation and chromatography and mass spectrometry as well as next gen sequencing technology for oncology testing and research. Our targeted growth initiatives tied to global broadband and energy efficient fuel cells are performing very well. Two great examples of how we are leveraging our tech in fast growing niche markets.

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The semiconductor market remains steady. We see customer-related supply chain issues driving some slowing, but we are offsetting this headwind through share gains. We provide consumables and technology to drive fab efficiency, buffering us for some of the CapEx slowdown on the new equipment side.

Our material processing business remained strong on continued pharma and biopharma demand. We are seeing some order slowdown due to investment delays by our customers, but our funnel remains strong and of high quality. Our HST industrial market performance is very much like the experience in FMT.

Finally, turning to our Fire, Safety and Diversified Products segment (sic) [Fire & Safety/Diversified Products segment] (13:23). Orders were flat year-over-year as a difficult quarter-over-quarter comparables in our dispensing business was offset by strong growth by the balance of the portfolio. Sales were quite strong with an organic increase of 14%. FSD adjusted operating margin expanded by 70 basis points versus the third quarter of 2021 driven by strong volume leverage partly offset by pressure on price/cost and higher employee-related costs. Although price/cost is still dilutive to margins, it did improve sequentially.

Our dispensing business performed well with the delivery of North American project volume and continued strength in the global architectural paint market. But orders were down 30% year-over-year due to large North American replenishment orders that we received last year. Within our fire business, OEMs continue to struggle with supply chain constraints, but we did see positive organic growth from price realization, improved execution and favorable performance in loose equipment. On the rescue side, we continue to win with our latest generation E3 tool, bringing enhanced tool features to the market.

Finally, BAND-IT experienced strong results across the industrial, automotive and energy markets. We continue to win share by having shorter lead times and material availability. On the auto side, we are outperforming the market by capturing share on new platforms and winning content on priority high volume vehicles. With that, I'd like to provide an update on our outlook for the fourth quarter and full year 2022.

I'm on slide 11, which lays out our updated guidance. For the fourth quarter of 2022, we are projecting organic revenue growth of approximately 9% and operating margin of approximately 23.5%. We expect that the volume will decrease sequentially from the third to fourth quarter due to normal seasonality and scheduled maintenance shutdowns. Q4 forecasted OP margin is down versus Q3 due to lost leverage on lower revenues. We expect GAAP EPS to range from $1.75 to $1.80 and adjusted EPS to range from a $1.92 to $1.97.

Turning to the full year. Given our strong performance in the prior three quarters, we are raising our full year guidance. We now expect full year organic revenue growth of approximately 12%. We expect GAAP EPS to range between $7.75 to $7.80 and expect EPS to range from $8.04 to $8.09. Our operating margin for the full year is expected to be approximately 24%. And we expect free cash flow as a percent of adjusted net income to range from 75% to 80%.

With that, I would like to turn it back to Eric for closing remarks.

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Thanks, Bill. As we wrap up, I'd like to share that my thoughts are with our Pulsafeeder team in Punta Gorda, Florida, who continue to cope with the aftermath of Hurricane Ian. All our employees are safe and our values shine through as our other IDEX businesses banded together to provide relief supplies to our colleagues there and our IDEX Foundation Board of Directors approved a large donation to the American Red Cross. Our facility did sustain some damage, but we have returned to operations. I would also like to extend my public

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congratulations to Katrina Helmkamp, who has replaced Bill Cook as the Non-Executive Chair of our Board of Directors. Bill Grogan and I have both worked closely with Katrina since she joined our board in 2015 and we look forward to continuing to lever her strong operating leadership skills and experience across multiple markets and technologies to drive IDEX forward. I'd also like to thank Bill Cook, who has been an invaluable contributor to our company, our board and my personal development throughout his 14-year tenure.

With that, I'll turn the call over to the operator for your questions.

QUESTION AND ANSWER SECTION

Operator: At this time, we'll be conducting a question-and-answer session. [Operator Instructions] Our first question today is from Mike Halloran of Robert W. Baird. Please proceed with your questions.

Michael Patrick Halloran
Analyst, Robert W. Baird & Co., Inc.

Q

Hey. Good morning, everyone.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Good morning, Mike.

Michael Patrick Halloran
Analyst, Robert W. Baird & Co., Inc.

Q

So, couple questions here, more on the demand order side of the things. First, on the order side. Flattish orders against really tough multi-year stacked comps here. Seems like a good outcome, sequentially lower. When I think about those order numbers, is there anything in there from a weakening perspective we should think about? And then, how much of that sequential change is seasonality or just a normal air pocket that develops as lead times start normalizing to kind of historically normal levels?

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Yeah. I mean, you hit a lot of the elements there. I mean, there's a piece of this that we always suspected was going to be there as we start to come off of an incredibly high backlog positions, especially for a short cycle, quick lead time business like ourselves. So, there's a piece of it that no doubt will be that and we'll keep an eye on the rate of travel of it as it runs out. There is some summer – kind of summer months' seasonality that's in there as well. I would say from a categorical softness standpoint, probably the one area we'd point to that covers a lot of IDEX businesses would be just some general softening on the European front, which probably isn't too surprising. And then I'm sure we'll talk later here about projects – large projects and things of that nature.

They – that's an interesting story. I mean, they were – beginning of this whole recovery, I mean, there was a lot of caution on people's part, sort of held them back. I think in the middle part or lot of the duration honestly there was just not enough time and energy to get at it or resources. And now you're kind of seeing that tilt back. Probably it is more of a cautionary tone again. We got a few things that have moved out and placed themselves, decisions into Q1 of next year, things of that nature as well. So, few things that we can point to, some things that are sort of

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normal based on where we are from a backlog position and time of the year, but underneath and around all of that, really, really strong support across the board.

Michael Patrick Halloran
Analyst, Robert W. Baird & Co., Inc.

Q

Thanks for that. Super helpful. And in the prepared remarks, you talked about the ability for IDEX to manage with whatever kind of environment [indiscernible] (20:06) in 2023, and certainly your track record supports that pretty aggressively. What is the base case as you guys are thinking about it today as we move into next year? Obviously, we've talked a lot about the need and the opportunity for a strong industrial cycle. Doesn't mean you can't get some weakness as we move into next year. So, as you look through your pretty varied end markets going into next year, how are you thinking about that set up and what's the opportunity set for growth?

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Yeah. Well, look, I think, as I said in the prepared remarks, you could see a few paths that would run out here. I mean, one that's more positive, something that's short term and kind of a short term pullback. And then, obviously, maybe something with a catalyst that's more negative that none of us can imagine. I just always come back. When we talk about that in the company, I mean, we literally scenario-play every one of those. We understand kind of what's variable, what's not variable across all our businesses. We always go back to the top growth bets in the company, almost all of which we can kind of see traveling across the duration here. We factor that in as well.

We've certainly learned a lot like every company about how low you can take discretionary spend, in many ways lower than we would have thought possible before. We know where that floor is and kind of how we would stack that against any of those scenarios. We talked for a while on the head count side, we'd be careful. Talent is hard to get. I mean, we're not really at a flush position there anyways. We're actually still pretty lean. I mean, we'd be very careful there. And then, honestly, we would rotate towards the strong, and we'd go pretty lean on areas that are weaker.

And so [ph] I don't want to be (21:44) too predictive here because I think it's still pretty variable in our minds, but our approach to each one of those paths is not. We actually know exactly what that is.

Michael Patrick Halloran
Analyst, Robert W. Baird & Co., Inc.

Q

Thanks for that. Really appreciate it.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Thank you.

Operator: Our next question comes from the line of Nathan Jones with Stifel. Please proceed with your question.

Nathan Jones
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Good morning, everyone.

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Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Hey, Nathan.

Nathan Jones
Analyst, Stifel, Nicolaus & Co., Inc.

Q

I wanted to start with some price/cost discussion. You guys have said that price/cost and – has been dilutive to margins in 2022. Is that something you target recapturing in 2023? As we've started to see costs moderate, do you believe you can recapture that margin that was lost in 2022 to price/cost?

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Yeah. No, definitely. As we said in the prepared remarks, we're back to our historical levels here in the third quarter as we continue to ramp our price capture. Inflation hasn't gone down, but it's moderated a bit. So as we look forward to the stickiness of the price that we implemented here as we progress through 2022, that sticking in 2023, optimistic about our ability to keep above our historical levels.

Nathan Jones
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Okay. And maybe you could just talk a little bit about some of the order cadence in your shortest cycle businesses. I know you guys have a few businesses that tend to be canaries in the coal mine. I think you said BAND-IT still remains pretty strong. But any commentary you can give us on those businesses that you consider to be leading indicators of the order cadence there?

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Yeah. They're still really strong. I mean, they have held steady, many – in many places, and there's four or five of them, we've done a really nice job on putting some strategic inventory together. Our natural ability to replenish fast has allowed us to go capture some share and some orders and then turned them and converted them to sales pretty quick on top of it. So, no real pressure signs coming from that very short cycle stuff that we always talk about. We look at that constantly. That's holding up. There's still an awful lot of demand for it, a lot of capacity that's got to lay in and it's always been pretty indicative of kind of the level that the industrial machine is working at because a lot of it is one-for-one replacement. And I think – I mean, all of our plants are working pretty fast and I suspect that's the case out in a lot of the places we supply to. So, that's holding up well.

Nathan Jones
Analyst, Stifel, Nicolaus & Co., Inc.

Q

And one last one, just on your own inventory levels. Obviously, everybody's been carrying a bit of extra inventory through these disrupted times. Plans on where you think that goes to in 2023 and what kind of cash generation we should be looking at for next year?

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Yeah, no, the third quarter was the first time in the last several that we actually didn't build an incremental inventory and we've start – we've stabilized them at current levels and look to bleed here in the fourth quarter, progressing into the first half of next year. Obviously we said our long-term goal is to be at over 100% cash flow

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conversion and I think we'll progress to that level over the next couple quarters. First half is always a little bit light from a cash flow perspective, on timing and we're more back half loaded, but we look to continue to progress our inventory balances down here over the next six months.

Nathan Jones
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Thank you very much for taking my questions.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Thanks, Nathan.

Operator: Our next question comes from the line of Deane Dray with RBC Capital Markets. Please proceed with your questions.

Deane Dray
Analyst, RBC Capital Markets LLC

Q

Thank you. Good morning, everyone.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Hi, Deane.

Deane Dray
Analyst, RBC Capital Markets LLC

Q

Hey, like to follow up on Nathan's last question there for Bill. Is there any way to quantify the inventory that you're carrying that would be considered more buffer inventory that as lead times begin to normalize, you can start to sell that down? And then Eric just talked about being aggressive with the opportunity on some of the fast short cycle businesses that the inventory ready to go. So – and that's kind of would be offsetting to that. But can you quantify for us what that opportunity would be to normalize working capital?

William K. Grogan
Senior Vice President & Chief Financial Officer, IDEX Corp.

A

I think internally we're targeting to get somewhere between 0.5 turn and 1 turn as we progress to our more historic levels. The buffer inventory is probably at the lower end of that. We'll keep some of that as the businesses look on the strategic side where we've been able to take share with some of that inventory level, we'll keep that and the focus is just as we've built up inventory to buffer and/or have had to increase inventory levels based upon quantities we had to commit to or customers that have paused some of their shipments as they've worked out supply chain issues on their side and we've built up a little bit of finished goods. Those parts will be the first part to bleed and the things that we think are strategic to enable some of the share capture, we'll hold on to that.

Deane Dray
Analyst, RBC Capital Markets LLC

Q

All right. Good. That's helpful. And then can we just go through at whatever level you'd like to share the whole cancellation of the customer COVID test application? I think you framed for how it was – how that came about and

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the impairment that you took. Is that the end of it in terms has it been completely written off? And you did include it in your operating results, which we appreciate.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.
A

Yeah. That's the end of it. I mean there's some small shipments here in the fourth quarter, but fundamentally it was an initiative that we started and highlighted back in 2020. We partnered with that customer and had a great relationship relative to that partnership on developing the technology and them committing a significant amount of capital support or production capabilities and obviously as they've moved in a different direction, have got out of the testing, caused the impairment and then the recognition of all the deferred revenue here within the quarter. So, most of the noise is – had been taken here in the third quarter. We've kind of moved past with significant knowledge gained in terms of production capabilities and technology that we'll continue to leverage as we move forward.

Deane Dray
Analyst, RBC Capital Markets LLC
Q

That's real helpful. Thank you.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.
A

Sure.

Operator: Our next question comes from the line of Allison Posniak (sic) [Allison Poliniak] (28:03) with Wells Fargo. Please proceed with your question.

Allison Poliniak-Cusic
Analyst, Wells Fargo Securities LLC
Q

Hi. Good morning. Eric...

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.
A

Hi, Allison.

Allison Poliniak-Cusic
Analyst, Wells Fargo Securities LLC
Q

...would love a little more color on the decision to align FSD and FMT under one leader. Does that indicate sort of maybe potentially more divestitures as you kind of look to refine the portfolio going forward? Just any thoughts there?

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.
A

No. Appreciate the question. What I was really trying to emphasize in the remarks is we're looking for a leader with, frankly, experience, scale and depth of experiences and a broad reach, which would line up well with where we want to go as a company. And so by sort of combining those businesses, at least under her watch, it allows us to essentially position the skill, attract somebody of that caliber and put somebody on the team that's honestly got some experience in some of the areas where we want to go. It's completely about that. Everything else

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underneath Melissa is identical to what we've seen before. We kept it very separate and distinct. We run it exactly the same, but it allows one person to come out of the team with some very, very good capabilities.

Allison Poliniak-Cusic
Analyst, Wells Fargo Securities LLC
Q

Great. And then, Bill, just going back to the HST orders, I think you kind of alluded to the fact that they were just – there were some orders that were essentially just pushed to Q4. Have they been executed on, have they turned into orders or is it something we're still waiting to come forward here?

William K. Grogan
Senior Vice President & Chief Financial Officer, IDEX Corp.
A

Yeah. No, not yet. The teams are still negotiating final pricing for things going into next year. So, if we get them in Q4, first part of Q1, we'll get them, it's just a matter of timing.

Allison Poliniak-Cusic
Analyst, Wells Fargo Securities LLC
Q

Great. Thank you.

William K. Grogan
Senior Vice President & Chief Financial Officer, IDEX Corp.
A

Sure.

Operator: Our next question comes from the line of Brett Linzey with Mizuho. Please proceed with your question.

Brett Linzey
Analyst, Mizuho Securities USA LLC
Q

Hi. Good morning, all.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.
A

Hi, Brett.

Brett Linzey
Analyst, Mizuho Securities USA LLC
Q

Hey, was hoping you might be able to parse out how you're thinking about accretion this year and next on a carryover basis for the two recent acquisitions, Muon and KZ?

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.
A

In terms of incremental EPS?

Brett Linzey
Analyst, Mizuho Securities USA LLC
Q

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Yeah. So EPS accretion baked into the guide for this year, and then what you're thinking about for next year carryover?

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.
A

This year just a couple cents here in the back half and then we'll have a couple cents there in the first half of next year as it'll comp as we progress into Q3 and Q4.

Brett Linzey
Analyst, Mizuho Securities USA LLC
Q

Okay. Great. And then I was hoping maybe you could just give a little bit of color on the regional dynamic within orders and then specifically what the pace of that looks like through the quarter on a monthly basis and what you're seeing in October in Europe specifically?

William K. Grogan
Senior Vice President & Chief Financial Officer, IDEX Corp.
A

I'm sorry, Brett, the cadence of orders within each month in the third quarter?

Brett Linzey
Analyst, Mizuho Securities USA LLC
Q

Yeah. I was thinking more on a regional basis what the cadence of monthly orders was and how that progressed into October as well...

William K. Grogan
Senior Vice President & Chief Financial Officer, IDEX Corp.
A

Yeah.

Brett Linzey
Analyst, Mizuho Securities USA LLC
Q

...by the different regions.

William K. Grogan
Senior Vice President & Chief Financial Officer, IDEX Corp.
A

I would say the third quarter has got some seasonality historically relative to European holidays and slowness within August. Relative to normal order patterns [indiscernible] (31:19) anything that was a significant outlier relative to what we've seen over the years. As Eric talked about, fundamental orders in our book and ship businesses were strong throughout the quarter. They continue to be strong here in October. Most of the softness, like we said, a little bit on the book and ship stuff in Europe, and then some of the project-related business and some of the ordering was probably the bigger item within our European geographical look. North America and Asia still remain really, really strong.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.
A

And October pretty consistent with what we saw in Q3.

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Brett Linzey
Analyst, Mizuho Securities USA LLC

Q

Okay. Great. I'll pass it along. Thanks.

Operator: Our next question comes from the line of Thomas Johnson with Morgan Stanley. Please proceed with your question.

Thomas Claes Johnson
Analyst, Morgan Stanley & Co. LLC

Q

Hi. Thanks. Congratulations on the strong quarter. I just had a question on kind of near term results here specific to the HST business. You provided some pretty helpful commentary for us on some of those main drivers, the lower productivity and some of the discretionary investment that offset volume and improving price/cost from a margin standpoint in 3Q. So it would be helpful if there was any way that you could kind of quantify how that impacted EBIT margins on a sequential basis, just trying to think through the evolution from 2Q to 3Q from those headwinds and maybe how you see that progressing moving through the remainder of the year? Thanks.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Yeah. Probably a highlight to some of the productivity challenges as we ramped on some of the higher tech stuff in a couple businesses within HST. Yeah, sequentially, was down versus the second quarter. We think it'll ramp back up here as the business continues to progress and normalize and get more efficient in several of the facilities. Then we'll see a pickup in the fourth quarter.

Thomas Claes Johnson
Analyst, Morgan Stanley & Co. LLC

Q

Great. Thanks. That's all for me.

Operator: Our next question comes from the line of Vlad Bystricky with Citigroup. Please proceed with your question.

Vladimir Bystricky
Analyst, Citigroup Global Markets, Inc.

Q

Good morning guys and thanks for taking the call.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Hey Vlad.

Vladimir Bystricky
Analyst, Citigroup Global Markets, Inc.

Q

Hey. So, can you just talk about – you've obviously talked throughout the recovery about taking some share given your ability to service customers and your availability. So, as we're starting to see supply chain constraints gradually ease, can you talk about how you expect share trends to evolve as some of your competitors who were maybe more hamstrung at times are coming back more online to normalized service levels?

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Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Sure. There's probably two elements there I want to cover. There's one that I would argue we kind of carry most days. We generally have shorter lead times than a lot of the people we compete against when things are in normal state. I mean we engineer the businesses to run that way. And it's kind of all set up there. What's actually happened for us here with a lot of the share capture over the last couple of quarters is we made some really sharp calls on some inventory that's pretty specific, highly technical and not in wide supply. [indiscernible] (34:41) see some things coming to businesses to their credit without frankly approval loops and things that we don't need in a company like ours, they said, hey, we know how critical this is, we can kind of see where it's going to go, we're going to lay some in.

And so almost all of the share capture that we talk about, you can kind of take it right back into very specialized material that we accumulated. So, I think that's important because otherwise you might just think it's very benign stuff and metal bits and brackets and things like that where we just have to have them laying around. That actually would normalize as things improve. This is actually very, very strategic inventory that these businesses accumulated. So, that's an advantage state out of the gate. That's what we're largely referring to here. But then as we go and things normalize, we normalize and maintain that advantage, the natural advantage we have in many of our businesses. So, it's just an area that we always emphasize. It's kind of been dramatically positive for us because of really, really good choices in businesses.

Vladimir Bystricky
Analyst, Citigroup Global Markets, Inc.

Q

Okay. That's really helpful color. And then maybe just, as we think about organic sales, obviously you've surprised to the upside here over the past couple of quarters and just raised your 2022 organic growth outlook. So, can you just maybe parse out a little more what's driving that better top line growth? How much of it is incremental, better pricing than you expected versus just better volume-driven growth?

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Well, yeah. I mean, it's – there are certainly components of outperformance that are here. So I'm glad that you're bringing that up. I mean, our pricing is the highest level we've had out -throughout the year. We've been pushing that continuously. This is the kind of environment where our differentiated products are going to command the highest level of pricing. So that is no doubt a component and that's competitively advantaged. We talk a lot about the top bets in the company, the top bets – growth bets. They're the highest quality we've had. And so interspersed in all of the numbers that we're talking about, you see great things like broadband and outer space and things we're doing in genomics and some of the things going on in water and precision ag and through FMT and now some acceleration that we've been waiting for in the fire businesses in FSD. So, those bets are layered in with higher unit of measures than we've seen historically on top of recovering markets and well-positioned businesses. That's kind of the entitlement that we have, really strong price capture and a great stack up of – that's across the company.

Vladimir Bystricky
Analyst, Citigroup Global Markets, Inc.

Q

That's helpful. Great quarter. Thanks, guys.

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Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.
A

Thank you.

Operator: Our next question comes from the line of Rob Wertheimer with Melius Research. Please proceed with your question.

Rob Wertheimer
Analyst, Melius Research LLC
Q

Good morning, everyone.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.
A

Good morning.

Rob Wertheimer
Analyst, Melius Research LLC
Q

So I just have a general question. I wonder if you might tell the – I guess the story of Muon Group acquisition and how it sheds light on your process, multiples and other opportunities you have, whether it soaks up a lot of the availability or whether you're still active. Just kind of walk through how – obviously, you've had pretty strong success in acquisitions lately and that's my and I'd just like to get color on how that transpired.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.
A

Yeah. Well, it's a business we've known for a few years. It's very much an IDEX business. I mean, it's a highly precise, niche component, doing wonderful jobs for a variety of high-end markets, including the ones we had identified in the prepared remarks. I gave the lot of credit to Marc Uleman, who I referenced in my opening remarks. It's a Netherlands based business. Marc is located in the Netherlands and he kept a very active cadence with his team over the last few years. We found a time and a space where we're able to generate some actionability and got the deal done, mainly because we could get our head around it very, very quickly based on the work we've done over the last few years and our familiarity with it.

What's great about a business like this one is and the reason I say it's so IDEX like, because it's actually very tunable. That's one of the reasons we like these precise components businesses. So it pings into some very high quality areas of semicon. There's some great applications in medical devices, food production – high-end food production. All areas that we study and participate in across the business, so we can leverage that insights and then apply it on a high quality niche business like this one.

Longer term down the road, this actually sits next to a lot of things we have in our scientific, fluidic and optics spaces. There's some commercial relationships that we could leverage there. There's actually some very interesting technical questions and things that we're going to explore together over a longer duration. And then honestly and when we think of value creation, we just start to apply the way we run things at IDEX. You can take a high quality business like that. We would start with 80/20. It's – not all applications are created equal. We have a way of thinking about that, that we can teach to others, things like value capture with customers. And we do that really well. And so there's a whole bunch of leverageable assets as well, just that you apply against an already very, very strong business that's got a demonstrated history of growth. So, I think we're really, really excited about

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it. I think it's indicative of the kind of things that we're looking at and looking for. And, yeah, we'll see – we'll certainly talk to you about it as we go.

William K. Grogan
Senior Vice President & Chief Financial Officer, IDEX Corp.
A

And then, Rob, to your capacity comment, I mean, after the completion of Muon, we'll have spent about $1.5 billion over the last two years with really taking on a minimal amount of incremental leverage. So we'll have $1.5 billion to spend here over the next 12 months with a robust funnel, a lot of actionable assets within that funnel.

Rob Wertheimer
Analyst, Melius Research LLC
Q

No, that was a comprehensive answer. Thank you. And any commentary on whether that's an abnormally large asset within your funnel or whether it's peppered through with big and small? And with that, I will stop.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.
A

Yeah, no, I mean, it's a little larger than we've seen before. But I mean the nature of these kind of high quality niches, they tend to be in very similar spaces and the kind of the top end of the size of them is actually relatively constant across even a wide variety of businesses that we have. So, a well-positioned business that seems closer to the top end in a high quality niche like we think about is often this size. So, it's a little higher than we've seen before, but there's certainly more of them like it out there.

Rob Wertheimer
Analyst, Melius Research LLC
Q

Great. Thank you.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.
A

Thank you.

Operator: Our next question comes from the line of Matt Summerville with D.A. Davidson. Please proceed with your question.

Matt J. Summerville
Analyst, D.A. Davidson & Co.
Q

Thanks. Just a couple quick ones here. With FSD, how far behind is that business in terms of price/cost, meaning how much more margin can we look forward to as you fully close that gap? And then sticking with that business, on the dispensing side, how much of a revenue hold should we expect in 2023 from those big projects that revenued this year? And then I have one follow-up.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.
A

Sure. I think we look for FSD to continue its ramp. We had said last quarter it had bottomed out and it will continue to progress as we move forward with the caveat that we still need to assess the project funnel for next year for dispensing. Right now, we don't think there's a huge hold. There'll be some softness on the replenishment side. If we weren't able to fill some of those larger projects, that would put a little bit of pressure on FSD margins

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relative to the progress that fire rescue has made. So, right now, we're still evaluating the impact of what the project funnel is for dispensing and I'm sure we'll give you more detail here as we get into the guide in January.

Matt J. Summerville
Analyst, D.A. Davidson & Co.

Q

And then just a modeling question. The divestiture, that Knight divestiture, can you disclose the financial profile of that business?

William K. Grogan
Senior Vice President & Chief Financial Officer, IDEX Corp.

A

Yeah. I mean, it was less than 1% of revenue and obviously a non-material amount of profit for us.

Matt J. Summerville
Analyst, D.A. Davidson & Co.

Q

Got it. That's all for me. Thank you.

Operator: Our next question comes from the line of Scott Graham with Loop Capital Markets. Please proceed with your question.

Scott Graham
Analyst, Loop Capital Markets LLC

Q

Yeah. Hi. Good morning all and congratulations on another standout quarter. I have...

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Thanks, Scott...

[indiscernible] (43:25)

Scott Graham
Analyst, Loop Capital Markets LLC

Q

I have questions – just sort of a broad-based question on organic first. With the supply chain improving a little bit and several quarters ago, Eric, you were able to take your best guess at quantifying what the negative was, with the improvement in the chain, can you maybe quantify what the positive was on organic this quarter?

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

I think from a share of capture and things we're able to do. I mean...

Scott Graham
Analyst, Loop Capital Markets LLC

Q

Well, actually, trying to maybe, if share capture's part of it sure, but kind of more like backlog depletion, things getting out, that versus hung up in backlog that maybe you didn't expect, but I am assuming that there was a bit additive to organic from a better chain.

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Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

I think it's a small amount, Scott. I think we've stabilized relative to our production output levels. As you look at where we've been from a revenue perspective, it's slightly elevated, so 1 point or 2 at most. We burned a little bit of backlog within the quarter, but backlog position is still pretty...

William K. Grogan
Senior Vice President & Chief Financial Officer, IDEX Corp.

A

High.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Pretty high.

William K. Grogan
Senior Vice President & Chief Financial Officer, IDEX Corp.

A

And it was a pretty minor burn there.

Scott Graham
Analyst, Loop Capital Markets LLC

Q

Got you. Okay, great. That was helpful. Thank you. Also – and I hope this doesn't count as a follow-up. What was pricing? I didn't hear it if you said it.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

No, no, we didn't. So, second quarter, we were at 4%. We ramped here in the third, little over 5%.

Scott Graham
Analyst, Loop Capital Markets LLC

Q

Okay. Thank you. And then just a question about [ph] the awarded (45:00) business. It's a pretty big business. You called it out as a certainly an area of strength and can you kind of talk about the dynamics of the growth in the quarter and is that a market that maybe would be a clear sort of green shoot market for you next year as well?

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

I mean, it's a good market. I always remind people that the work that we do there is on the analytical side, supporting whether – the infrastructure's ability to work well. So, that kind of work, I mean, it maps well with a lot of the digital solutions that are out there, that's where some of our more digital businesses are. So, [ph] robo crawlers (45:36) and flow monitorings to prevent overflows and things that could harm the environment. That's the work that we're doing, the bulk of it. Of course made an acquisition to deepen that here recently. So, we got some very good assets that in, we think, long term, obviously, there's no question the work needs to be done. It's long overdue. Yeah, there's a decent amount of stimulus and government support that's out there that always takes longer to find its way into projects than people imagine, but that frankly extends it over multiple years too. So, it just we kind of put that in a positive side. I'd agree on the green shoots side of it. We're very, very well positioned. We're doing – continuing integration work with the acquisition that we have to deepen all of it in our major geographies, and we view it as very favorable.

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Scott Graham
Analyst, Loop Capital Markets LLC

Q

Got it. Hey, thanks again.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Thank you.

Operator: Our next question comes from the line of Joe Giordano with Cowen. Please proceed with your question.

Q

Good morning. This is [ph] Michael (46:35) on for Joe.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Hey, [ph] Michael (46:38).

Q

In the prepared remarks, you mentioned strength around energy. Can you just dive a bit into the LNG outlook for FMT and if there's any future alternative energy opportunities? I know historically that's been an area of inorganic growth.

Eric D. Ashleman
President, Chief Executive Officer & Director, IDEX Corp.

A

Yeah. Well, I mean, I think our energy businesses have recovered pretty nicely throughout the year. I mean we've seen a few – we don't have a ton of upstream presence, but that's been stronger here lately. I think the midstream has got some delays and things on the project side and supply chain, some of the classic stuff, but probably lines up behind it because there's some things that are overdue there. And we've got – I mean, we've got kind of a classic custody transfer business, a lot of it's fossil fuel dependent with the current assets. A lot of that technology we're actually asking all the questions, as you might imagine of how transferable it is to other alternate energy sources and things that might be out there. Whatever it is, whether it's hydrogen or some other gases and liquids, it's going to need – people are going to need to get paid and we're going to need to measure that custody transfer happens. And that's kind of work that we long have done and are excited about.

There are actually other areas of IDEX that map against some of those same vectors in a way that probably would strike folks from the outside as kind of unusual as well. That's one of the ways we think of a trend like that is we kind of draw lines and tentacles into different verticals within IDEX, and then we sort of leverage insight around how the work is done, how things are shaping up and then distribute it across a variety of IDEX businesses that might be involved. They may not be going to market together. They might not even be in the same room. But actually some of the same dynamics are meaningful for them in terms of why they would want to invest in it. So, it's an area of interest for us in terms of how this will ultimately play out over time. But I think, for now, the kind of core things that we have are doing pretty well with a decent road and runway ahead.

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Q

Thanks. That's helpful. And just – and one follow-up if I may. Are there any product adjacencies that – within the energy sphere that you see more favorable and if this is something that's sort of in the funnel for the next 12 months or so?

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

A

I mean we've got some great projects there. They, as you might imagine, go very, very niche, very, very quickly. As an example, we've got a great application that makes sure that when you offload a railcar with propane, you get all of it out of the bottom. I mean seems kind of funny. You'd suspect – everybody would suspect that actually happens, it doesn't. So our team developed something that guarantees that 100% of the fuel is taken out of the car and then that's available as productivity for a variety of people. So it's that kind of work, that's sort of the – that's the unit of measure of things we think about and develop for customers. And there are others along the way but that's just one we happen to take a look at about a month ago, it's really, really interesting.

Q

Thank you.

Operator: That's all the time we have for questions. I'd like to hand the call back to management for closing remarks.

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Well, thanks. I appreciate the comments and the reflection on what we think was a very strong quarter here. For any of the IDEX team members that are listening, I want to thank you all again personally for your hard work and certainly difficult circumstances, a lot of change happening quarter-over-quarter, month-over-month. But as I said in the end of my remarks, this is the company where we really lean into that. Anytime the world gets difficult or problems worth solving and when they – and when we solve them with well-positioned businesses, I mean, it's a huge financial benefit for ourselves and our shareholders. So thanks for your interest. Look forward to talking to you more along the way.

Operator: Ladies and gentlemen, this does conclude today's teleconference. Thank you for your participation. You may disconnect your lines at this time and have a wonderful day.

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