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IDEX Corp. (IEX)

Q1 2023 Earnings Call

CORPORATE PARTICIPANTS

Allison S. Lausas

Chief Accounting Officer & Vice President, IDEX Corp.

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

William K. Grogan

Senior Vice President & Chief Financial Officer, IDEX Corp.

OTHER PARTICIPANTS

Deane Dray

Analyst, RBC Capital Markets LLC

Michael Patrick Halloran

Analyst, Robert W. Baird & Co., Inc.

Allison Poliniak-Cusic

Analyst, Wells Fargo Securities, LLC

Nathan Jones

Analyst, Stifel, Nicolaus & Co., Inc.

Vladimir Bystricky

Analyst, Citigroup Global Markets, Inc.

Jeffrey Todd Sprague

Analyst, Vertical Research Partners LLC

Will Jellison

Analyst, D.A. Davidson & Co.

Brett Linzey

Analyst, Mizuho Securities USA LLC

Joseph Giordano

Analyst, TD Cowen

MANAGEMENT DISCUSSION SECTION

Operator: Greetings and welcome to the First Quarter 2023 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.

And it is now my pleasure to introduce to you, Allison Lausas, Vice President and Chief Accounting Officer. Thank you, Allison. 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 our discussion of the IDEX first quarter 2023 financial highlights. Last night, we issued a press release outlining our company's financial and operating performance for the three months ending March 31, 2023. 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 will begin with Eric providing an overview of the state of IDEX's business. Then, Bill will discuss IDEX first quarter financial results, an update on segment performance and the markets they serve,

and our outlook for the second quarter and full year 2023. 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 13734462 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. I'd like to start with some key first quarter highlights. We delivered record sales with positive organic growth across all three of our segments, \$2.09 adjusted earnings per share and strong free cash flow. Our FMT and FSD segments performed exceptionally well, both achieving record sales and strong profitability, offsetting some pressure in our HST segment. Price/cost was positive and above IDEX historical performance.

As we look ahead to Q2 and the balance of the year, our outlook has changed. The last time we spoke, we anticipated short-term volume pressures within life sciences from inventory calibration concentrated in a few select OEM customers. However, as we progressed through the quarter, we saw signals of a broader, more prolonged recalibration within our HST segment, largely centered in our analytical instrumentation, life science, pharma and semiconductor markets. End market demand is still positive, but we believe our customers have sufficient inventory of our critical components to support their needs in the near-term.

Over the past two years, we experienced robust growth in HST, with sales up over 30% organically to support strong end user demand and customer-specific inventory replenishment. But as supply chain conditions improve and the broader demand profile normalizes, our OEM partners are aggressively attacking higher inventory levels, beginning with those suppliers that have demonstrated the quickest returns to pre-pandemic lead times. The sharp and simultaneous nature of this inventory recalibration exceeds all prior historical cycles. In response, we proactively executed cost reductions to offset a portion of this volume impact.

We tailored our approach to the specific challenges in individual businesses, as well as broader discretionary costs across the entire company, managing through the short-term, but not losing focus on our longer term growth path. These top line challenges, net of our cost containment plan, drive \$0.25 of adjusted EPS headwind for the year. Therefore, as we noted in our press release, we revised our full year adjusted 2023 EPS guidance from (sic) [to] (00:04:29) \$8.25 to \$8.55. Bill will discuss the specifics in greater detail during our segment and guidance updates.

Regardless of these end market challenges, we remain confident in our ability to deliver total shareholder returns over the long-term. Our capital deployment plan remains consistent. We continue to look to M&A as a significant source of value creation. To that end, we announced our intent to acquire Iridian Spectral Technologies for CAD 150 million or approximately \$111 million. Iridian is a world leader in custom optical filter solutions serving the space, life science and telecommunications markets.

Iridian expects fiscal 2023 revenues of CAD 36 million and EBITDA margin in the low-30s range. It is about a 13 times EBITDA trailing deal, and within the IDEX family of businesses, Iridian complements and expands upon the

solutions provided by our scientific fluidics and optics businesses within HST. This transaction is expected to close in the second quarter. Iridian will be our sixth acquisition since the beginning of 2021, and we remain bullish on our ability to deploy capital on high-quality assets, irrespective of the macro conditions.

The integration of our Muon Group acquisition, which closed in fourth quarter 2022, is progressing well. We've deployed key elements of our operating model, and there continues to be a strong cultural fit between IDEX and Muon, as our teams work together to unlock value between our businesses. Finally, I traveled last week to India to officially open our second plant in the State of Gujarat. It is a world-class facility that effectively doubles our production capacity in that country. Coupled with the opening of our plant expansion in China in late 2022 and our recent commissioning of sales and logistic centers in Singapore and Dubai, we now have a strengthened footprint to attack markets across Asia and the Middle East, a key element of our growth strategy.

With that, I'll turn it over to Bill to discuss our financial results.

William K. Grogan

Senior Vice President & Chief Financial Officer, IDEX Corp.

Thanks, Eric. Moving on to our first quarter consolidated financial results on slide 8, all comparisons are against first quarter 2022 unless otherwise stated. Orders of \$826 million were down 4% overall and down 10% organically, mainly driven by the timing of project orders for dispensing in FSD and next-gen sequencing in HST, as well as OEM pressure across the life sciences, analytical instrumentation, pharma and semiconductor markets in HST.

Record sales of \$845 million were up 13% overall and up 6% organically. We experienced 9% organic growth within our FMT and FSD segments and 3% growth in HST. Gross margin of 45.2% contracted by 40 basis points. This was driven by unfavorable mix largely centered in HST, the dilutive impact of acquisitions and employee-related inflation, partially offset by favorable price/cost and productivity.

Adjusted EBITDA margin, which includes \$6 million related to accelerated recognition of share-based compensation, was 27.2%, down 140 basis points. I'll discuss the remaining drivers of adjusted EBITDA on the next slide. Our effective tax rate for the quarter was 22.2% and was relatively flat compared with our prior effective tax rate of 22.4%.

Net income was \$140 million, which resulted in EPS of \$1.84. Adjusted net income was \$159 million with adjusted EPS of \$2.09, which was up \$0.13 or 7%. The accelerated recognition of share-based compensation that I mentioned earlier lowered adjusted EPS by \$0.06.

Finally, cash from operations was \$148 million and up 86%, primarily due to lower investments in working capital versus last year. Free cash flow for the quarter, which included higher year-over-year capital investment, was \$121 million, up 91% versus last year and coming in at 76% of adjusted net income. This represents the strongest first quarter free cash conversion we have experienced in the past five years.

Moving on to slide 9, which details the drivers of our first quarter adjusted EBITDA. Adjusted EBITDA increased \$15 million compared to the first quarter of 2022. Our 6% organic growth contributed approximately \$6 million flowing through at our prior year gross margin rate. Price/cost was accretive to margins, and we drove operational productivity that more than offset employee-related inflation. Mix was unfavorable by \$3 million, mainly centered in HST due to volume declines in our analytical instrumentation and life science components businesses.

Resource and discretionary spending increased by \$8 million. As we noted in our prior guidance, this was carry-over from last year. In 2022, we did not return to a sustainable level of discretionary spending until the second quarter. Equally, we ramped up our resource investment spend as we progressed through the year. This will come down as part of our cost mitigation plan for the balance of the year. We had \$6 million related to accelerated recognition of share-based compensation due to the timing of certain participants reaching retirement eligibility status.

These results yielded a 5% organic flow-through. Excluding the impact of accelerated share-based compensation, our organic flow-through was around 20%. Nexsight, KZValve and Muon acquisitions, net of the Knight divestiture and FX, contributed an additional \$13 million of adjusted EBITDA. Inclusive of acquisitions, divestitures and FX, we delivered 16% flow-through. Excluding the impact of accelerated share-based compensation, we delivered 22% flow-through.

With that, I'll provide a deeper outlook for our segment performance. I'm on page 10. In our Fluid & Metering Technologies segment, we experienced strong order and sales performance worth organic growth of 5% and 9% respectively. Adjusted EBITDA margin expanded by 50 basis points versus last year, driven by strong price/cost, volume leverage and productivity, which more than offset higher employee-related costs and discretionary spending, as well as the dilutive impact of acquisitions.

Industrial demand remained steady throughout the quarter. We experienced tailwinds from energy, mining, chemical and lithium-ion battery markets. Our water business has performed well. Quote activity remained strong due to US infrastructure funding initiatives, and we see continued momentum around the adoption of AI and cloud technologies. Our energy markets continue to be strong, driven by favorable oil export and mobile truck demand. In the chemical market, we are experiencing wins in the energy transition space, as well as strong China and Middle East demand.

The agricultural demand landscape is mixed. Farm fundamentals are positive with stable commodity prices and net farm incomes, as well as lower fertilizer costs versus last year. However, distribution inventory levels were higher than typical coming into the planting season, and a slower start to the season due to weather has delayed the turnover of this inventory.

Moving on to the Health & Science Technologies segment, organic orders contracted 23%, driven by the OEM inventory calibration impact, as well as timing of a large next-gen sequencing order we received in the first quarter of last year. As Eric noted, our life science and analytical instrumentation businesses are being impacted by broad-based inventory destocking, as our customers recalibrate to a more normalized demand pattern. We expect that these markets will continue to see this pressure through the second quarter, with some recovery in the back half of the year.

The semiconductor market is experiencing softness resulting from memory oversupply, as well as customers feeling the impact of US export controls. We anticipate that macro conditions will improve as we progress through the remainder of the year. We do continue to leverage share gain to buffer some of the broader market declines. Our material processing technology business is seeing softness across pharma, biopharma and nutrition markets, driven by tighter capital availability and customer hesitancy due to recession concerns. Our funnel does remain strong and we expect some recovery in the second half of the year.

The automotive market remains positive. We continue to see a solid global trend towards electrification, driving opportunities for our growth. We delivered 3% organic sales growth in the first quarter, driven by strong next-gen sequencing, satellite broadband and fuel cell targeted growth initiatives with some offset from the market factors I

mentioned earlier. Adjusted EBITDA margin contracted by 300 basis points versus the first quarter of 2022. Most of this pressure is in the gross margin line, with unfavorable volume leverage and mix more than offsetting favorable price/cost. The recent Muon acquisition is accretive to HST's overall EBITDA margin.

Finally, turning to our Fire & Safety/Diversified Products segment, organic orders contracted by 4%, mainly driven by timing of project orders in our dispensing business last year. Organic sales results were strong at 9% growth, with double-digit growth in both fire and rescue and BAND-IT, offsetting the decline in dispensing. Adjusted EBITDA margins expanded by 160 basis points versus last year, largely driven by strong price/cost performance, volume leverage and productivity, more than offsetting higher discretionary spend and employee-related costs.

The paint market is mixed, with pressure from the North American replenishment cycle coming to an end and softness in Southeast Asia, being offset with strong European and Indian demand. Within our fire business, demand for trucks remains strong. North American OEM volumes continue to be constrained by supply chain. However, we are gaining share with North American mid-tier and China OEMs with our integrated systems strategy and have pivoted our go-to-market approach for our SAM product to retrofit in-service trucks to bypass the OEM backlog constraints.

Our rescue markets are stable, and we have experienced favorable demand in Europe and good project activity across most of the globe. BAND-IT results continue to be positive. Industrial demand is steady, energy is strong, and we continue to drive higher-than-market performance in automotive due to our position on high-demand vehicles and share gain. With that, I'll give an update on our outlook for the second quarter and full year 2023.

I'm on slide 11. I'll now provide some additional details regarding our revised 2023 guidance for both the second quarter and the full year. In Q2, we are projecting GAAP EPS to range from \$1.86 to \$1.89 and adjusted EPS to range from \$2.10 to \$2.13, with organic revenue growth of approximately 3% and adjusted EBITDA margins ranging from 27.3% to 27.7%. We anticipate that HST volumes will be negative in the second quarter and the strength we saw in Q1 industrial performance sustains.

Turning to the full year, as Eric mentioned, we have reduced our full-year revenue guidance reflecting headwinds related to OEM destocking across the HST segment. At the midpoint, we expect volume and mix impact reduces EPS by \$0.48, offset by \$0.23 of cost actions, yielding \$0.25 of net pressure on our annual guide. This equates to a full-year low single-digit organic revenue contraction in HST and low to mid-single-digit growth in FMT and FSD. Our view on the industrial market has not changed, and we continue to assume a second half decline with a modest recovery in the back half for HST.

Bringing it all together, we project GAAP EPS of \$7.30 to \$7.60 and adjusted EPS to range from \$8.25 to \$8.55. We expect full year organic revenue growth of 0% to 3% and adjusted EBITDA margin to range between 27.5% and 27.9%. The high-end of our range implies that we will sustain our record profitability from last year. Capital expenditures are anticipated to be about \$70 million and free cash flow is expected to be 100-plus-percent of adjusted net income.

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

QUESTION AND ANSWER SECTION

Operator: Thank you. We will now be conducting a question-and-answer session. [Operator Instructions] And our first question comes from the line of Deane Dray with RBC Capital Markets. Please proceed with your question.

Deane Dray

Analyst, RBC Capital Markets LLC

Thank you. Good morning, everyone.

Q

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Hey, Deane.

A

Deane Dray

Analyst, RBC Capital Markets LLC

Hey. Just starting with the HST story here, and look, we're seeing this across the sector. We cover Danaher. They've been through this whole kind of you're on the other side of the COVID surge in volume, and Dover's Biopharma Pumps, same story there as well. So, it's not execution. We know that it's not share loss. But what's your degree of confidence in the path to normalizing? Just what kind of visibility do you have here?

Q

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Well, thanks, Deane. I mean, I'd say a couple of things. One is you'd expect, given the magnitude of some of the swings – I mean, the discussions and the intensity and the iteration of them within customers at all levels, commercial operations is probably at the highest level we've ever had. And then, I would say, as you look at the actual order intake, you can see some things firming up in the back half. So, you can see actually kind of the same planning and methods that are pulling it down now are actually repositioning it a little further out in the later – in the year, sorry. And you're seeing that for the kind of standard products that we would usually gauge that are kind of right down the middle of the volume fairway. So, it deviates a little bit market from market. But I'd say those two factors are probably the two that we're most reliant on as we think about that.

A

Deane Dray

Analyst, RBC Capital Markets LLC

All right.

Q

William K. Grogan

Senior Vice President & Chief Financial Officer, IDEX Corp.

Deane, as – and I'd just add, as our guide, on the low-end, we have kind of that HST recovery only up about 1% sequentially from the first half to the second half. And then, on the high side, 7%. So, reasonable range relative to the things that Eric just highlighted.

A

Deane Dray

Analyst, RBC Capital Markets LLC

Q

All right. That makes sense. Appreciate that. And then, second question, and Eric, maybe you can bridge the comments from last quarter about uncertain period of softness, how that's been playing out here, as well as the trends you're seeing across your short cycle businesses, the implications, day rates, lead times, and so forth.

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

A

So, are you are saying, Deane, kind of take it from a little bit more depth on the HST and then [indiscernible] (00:20:12).

Deane Dray

Analyst, RBC Capital Markets LLC

Q

No, no, no.

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

A

Okay. Yeah.

Deane Dray

Analyst, RBC Capital Markets LLC

Q

Just broadly for IDEX. Your comment last quarter about uncertain period of softness. We're all seeing pockets of softness. But I wanted to see, with a quarter through now, what trends you're seeing in the short cycle.

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

A

Got it, specific there.

Deane Dray

Analyst, RBC Capital Markets LLC

Q

Are you seeing any of that in day rates and lead times or so forth? Thanks.

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

A

Yeah. So, obviously, the most pronounced recalibration happening exactly in the area that we're talking about here in HST. As you look at the industrial side of it and in particular kind of the day rate stuff right down the center of our fairway, first quarter held up really, really well. I mean, business to business, I think we called out ag is the only one where we saw some similar dynamics of kind of inventory and things ready to go to plan.

I will say though in more recent data here in April, some of those canaries that we often reference, you can see things pull back a little bit and you can see them doing it together. So, it is going to be something we'll watch. April, for whatever reasons, never a real strong predictor for us. It firms up as we go through May and especially into June. But I will say you can see a little bit of that there in those businesses in terms of just day rates. It's not a big drop, but the uniformity of it is interesting across a couple of weeks here most recently.

Now, when you kind of hold that up with some other things, some of which we do informally and others have done more formally around inventory positions of distributors and things like that, you can see sort of the same comments hold that up with the same feelings of uncertainty. So, it's not a logic break in terms of how this might

play out. And let's remember, in our comments here last time, I mean, we actually had this positioned in our back half. So, we have a bit of a glide path and I've here very recently seen some of the first signs of it.

Deane Dray

Analyst, RBC Capital Markets LLC

Q

That's really helpful. But just to clarify, when you talk about the leading indicator canaries, that's like BAND-IT and Warren Rupp and [ph] GAS (00:22:15)?

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

A

Yeah. And a couple of the other FMT pump businesses, and even more specifically, a couple product lines we look at within them, where we just know they tend to be ordered typically one and two and three general replacement. The ones you mentioned, few other places. But yes, they're the ones we often always look at when we talk to you.

Deane Dray

Analyst, RBC Capital Markets LLC

Q

Thank you.

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

A

Thanks, Deane.

Operator: And the next question comes from the line of Michael Halloran with Baird. Please proceed with your question.

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

Hi, Mike.

Michael Patrick Halloran

Analyst, Robert W. Baird & Co., Inc.

Q

Can we follow up on Deane's question and talk about the other side of the coin, just maybe the CapEx side of things? Are you seeing any pullbacks? Obviously, ignore some the destock HST stuff you already commented on. But on some of the other longer cycle pieces, are you seeing any change in dynamic or anything noteworthy underneath the hood?

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

A

Well, if – these are the larger projects that we sometimes talk about here. I mean, we have them in two places and they're a little different. So, I think they're more pronounced – more aggressive on the HST side in the markets that we're referencing here. So, you can see some concern in places like MPT.

Michael Patrick Halloran

Analyst, Robert W. Baird & Co., Inc.

Yeah.

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

We referenced those in the comments. But let's tie those to that sort of general macro story that Deane did a good job framing for us. I think on the industrial side, I would just kind of come back and say, the entirety of this cycle, it's not been a big piece of our story. I remind folks, in the beginning of the ramp-up post-COVID, there was a lot of uncertainty there. Frankly, that turned into the inability to put those projects together. Then, as inflation came about, there was a repricing element that sort of prevented some of them from our side. And now, yeah, maybe we're drifting a bit more into uncertainty too. So, [indiscernible] (00:24:04-00:24:22) quite positive for us, not really because of large projects, just that sort of general day-to-day business is doing real well.

Michael Patrick Halloran

Analyst, Robert W. Baird & Co., Inc.

All right. Thanks for that. And apologies in advance for this one. I think Bill gave some commentary on expectations by the segments for the remainder of the year. Unfortunately, you guys were breaking up on me. Could you just repeat that in case I misheard? Or maybe I'm wrong, maybe you guys didn't do that. But can you comment on that?

William K. Grogan

Senior Vice President & Chief Financial Officer, IDEX Corp.

No, no, no. We did. In our updated guide, the implied organic revenue for HST is negative low single-digits, and for FMT and FSD positive low single-digits.

Michael Patrick Halloran

Analyst, Robert W. Baird & Co., Inc.

Okay. Okay, that's helpful. And then, I guess just the quick follow-up on that then, on the FMT piece, the orders are good. I think the end markets there are probably a little bit healthier broadly. Why the decel as you work through the year on that piece specifically? Is there anything you're seeing that's concerning or is it just how you think things layer out as we look forward?

William K. Grogan

Senior Vice President & Chief Financial Officer, IDEX Corp.

No. Exactly, I mean, it's been our stance as we came into the year, an expectation that the industrials were going to start to fall off in the back half of the year. We saw strength in the first quarter. We knew what our backlog positions were. And Eric just highlighted some of the caution we're seeing in our daily book-and-ship order rates that I think just give us more confidence in our call that the back half will be softer for those businesses, down a couple of percent on the volume side as we progress over the next quarter or two – post the second quarter, so positive here, yeah.

Michael Patrick Halloran

Analyst, Robert W. Baird & Co., Inc.

Yeah. No, no, thanks. I appreciate it, guys. Thank you.

Q

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Yeah.

A

Operator: And the next question comes from the line of Allison Poliniak with Wells Fargo. Please proceed with your question.

Allison Poliniak-Cusic

Analyst, Wells Fargo Securities, LLC

Hi. Good morning.

Q

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Hi, Allison.

A

Allison Poliniak-Cusic

Analyst, Wells Fargo Securities, LLC

Just keeping on FMT, can you touch on the acquisitions, KZValve and Nexsight, because it seems like they were exceptionally strong? Just want to better understand maybe the drivers there and sort of how we should think about those for the balance of the year. Thanks.

Q

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Yeah. I mean, holding up really, really well. KZ, just to remind people, brought a key piece of automation technology that frankly goes to the same customer set that we have in our Banjo business. They're very close by. So, I mean, this is [indiscernible] (00:26:46). And so, we're working the commercial side, the technical side, and all of the pieces of the IDEX operating model. So, really, really happy there.

A

The Nexsight business, reminder there was they were kind of long channel partners and there was a piece of software that came with that business we've long used as well. So, many people kind of associated this with IDEX for a number of years. So, pretty seamless integration, expands our presence and depth. And then, the water markets, as we referenced in the earlier comments and we'll say here, are doing well. There's good – strong support for municipal projects, municipal work that I think will play out for quite a while. So, yeah, real favorable with those two.

William K. Grogan

Senior Vice President & Chief Financial Officer, IDEX Corp.

Yeah. And KZ, their mix of business is much more concentrated towards OEM. So, they're not seeing some of the inventory issues that Banjo is.

A

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Yeah.

A

Allison Poliniak-Cusic

Analyst, Wells Fargo Securities, LLC

Got it. And then, just on the HST side again, I know you're looking for maybe a second half recovery from those inventory issues. But as we think about sort of that back half and then maybe even into 2024, does that sort of drive that growth somewhat below trend of what you would expect kind of going forward at least over the next 12 months? Just any thoughts there?

Q

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

You know, I don't think so. I think largely, this is a story of coming off of a multi-period really aggressive rates, both for us and our end customers. I mean, I look at our segment. I mean, HST was up 30% across two years. I think that tracks with a lot of the end markets where we are. And so, a retraction or a pullback down to more typical rates in the single-digits, even if they're mid-single-digits, is pretty dramatic if, in fact, your thinking is changing in a relatively short time horizon.

A

So, I think the single biggest variable for – certainly for us as a component supplier into it is going to be levels of inventory [indiscernible] (00:28:31-00:28:44). So, in some ways, it's doing math. It's math and rate of travel. It is different than we've seen before. But the preceding period and the run-up there was different as well. So, I think we're all learning to do that together. And as I spoke earlier on the call, the need for even tighter alignment and iteration as we go through that to protect everybody is very important.

Allison Poliniak-Cusic

Analyst, Wells Fargo Securities, LLC

Got it. Thank you.

Q

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

Nathan Jones

Analyst, Stifel, Nicolaus & Co., Inc.

Good morning, everyone.

Q

William K. Grogan

Senior Vice President & Chief Financial Officer, IDEX Corp.

Good morning.

A

Nathan Jones

Analyst, Stifel, Nicolaus & Co., Inc.

Couple questions on HST. I just wanted to hit the margins, down 300 basis points year-over-year in the first quarter. I think, Bill, you said – talked about lower absorption, but revenues were up 3% organically. Can you maybe just flesh out a little bit the inputs into the year-over-year margin decline in HST?

Q

William K. Grogan

Senior Vice President & Chief Financial Officer, IDEX Corp.

A

Yeah. I think the biggest driver, Nathan, is the mix impact. Some of the volume decreases we've seen are in our highest margin product portfolio in the business. That has somewhat offset that to keep the business positive from an organic perspective. And then, with the overall segment being positive, there are still some pockets that were negative that caused us to deleverage on some of the fixed cost side.

Nathan Jones

Analyst, Stifel, Nicolaus & Co., Inc.

Q

Okay. That makes sense. And then, just maybe a little bit more color on how you expect the year to sequence on HST. I mean, you had in the 20s of orders down. Just maybe any color you can give us on how we should think about the comps. I guess especially in 2Q, with this being a relatively short cycle business, do you take most of the pain here on organic growth in the second quarter and then you see revenues improve pretty meaningfully sequentially as we go past that?

William K. Grogan

Senior Vice President & Chief Financial Officer, IDEX Corp.

A

No, no. Relative to our backlog position, we will be negative in HST in the second quarter, but kind of low single-digits. And then, remember, the second half of this year was significant – or the second half of last year was significantly higher. So, we'll have a little bit of comp problems that will keep HST either flattish or slightly negative for the balance of the year.

Nathan Jones

Analyst, Stifel, Nicolaus & Co., Inc.

Q

And then, just one last one on HST. IDEX is not typically an inventory business. You're not typically seeing a lot of inventory on customer shelves. Obviously, an inventory destock is what we're talking about here. Can you just talk about how this inventory ends up on customer shelves? How that works its way through the system?

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

A

Yeah. No, it's a great question, Nathan. I mean, in general, everything we make here is pretty customized for a very specific end use, if not a specific single customer. And in the area that we're talking about in the health science world, I mean, that absolutely happens. These are spec'd in components. They don't travel east and west. When we're more generally talking about an IDEX, so FMT and then in that segment FSD as well, you've got a channel between us and all of these fragmented end markets, which are at much lower volumes. And so, no single one of them is going to tend to raise its head up at any one point.

So, that comment generally holds there. And while it's specific customized here, this is a highly concentrated customer set and it's a super direct transaction. So, if you chose to do it – and they don't often do it and this is a bit unprecedented. But if you chose to do it that way, you could put mission-critical components down that you know you're going to use because they're the most high running parts that you have in the system, even though they are absolutely customized for that customer only.

Nathan Jones

Analyst, Stifel, Nicolaus & Co., Inc.

Q

Okay. Thanks for the color.

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Yeah.

A

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

Vladimir Bystricky

Analyst, Citigroup Global Markets, Inc.

Good morning, everyone. Thanks for taking my call today.

Q

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Hi, Vlad.

A

Vladimir Bystricky

Analyst, Citigroup Global Markets, Inc.

So, I just wanted to ask you, in FMT, I think you, if I'm not mistaken, kind of upgraded your commentary around the strength of the energy and chemical performance you're seeing. I know you mentioned it's not really project activity yet. So, can you just talk a little bit more about where you're seeing improvements in demand in those end markets and how you're thinking about sort of the sustainability of that strengthening?

Q

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Yeah. Well, I think in energy specific, remember that we largely do mobile custody transfer there. So, there's a little bit of an overhang as the industry gets healthier and price support are out there, you're going to get some general tailwinds for CapEx spend. More specifically for us though, we do a lot in mobile applications, a lot of which depends upon chassis availability. That was highly constrained for a couple of years. That's freed up as a lot of other supply chains have, and some of it is just captive demand at a good and favorable time in the environment. That – something like that, a micro story like that actually matters for us.

A

On the chemical side, we've seen strength in China specifically with our Richter business. I think some of that is probably also related to the fact the country was kind of locked down for a while. There's some investments that have to be made. We're super well-positioned there. We'll see how that plays out longer term. And actually, Europe in the chemical side, which is an area of concern and was pretty depressed as well for a bunch of reasons we've talked about, that was actually pretty strong for us as well. So, it's these little pockets that kind of play out in typical IDEX fashion that go from big to small stories here, but I would say – and generally are still following others out there that are larger. So, not a massive component of project spend or multi-period expansion here, but more micro events and things, and otherwise, markets I think are doing pretty well.

William K. Grogan

Senior Vice President & Chief Financial Officer, IDEX Corp.

And then, I think the other thing is on the energy business, they've launched a couple of new products that have been very well-received in the end marketplace. And then, we talk about businesses that had some differentiation relative to their ability to have inventory to supply their customer base. I think a couple of businesses within our

A

valve that mostly sell into the chemical market have been well-positioned relative to their inventory that they've carried to take some share from their customers.

Vladimir Bystricky

Analyst, Citigroup Global Markets, Inc.

Q

Okay. That's very helpful. Thanks. And then, just on the M&A front, can you give us some more color on the Spectral Tech acquisition? I know it's relatively small. But can you just talk about what attracted you to that particular asset, potential scalability of the business, and more broadly, what you're seeing in the M&A pipeline and environment today?

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

A

Yeah, sure. So, the – I mean, the Iridian business, I mean, it's – as we said in the release, it's a leading designer and manufacturer of thin-film multi-layer optical filters. We do that in a lot of other places within IDEX, both in our optical technologies segment and some of it embedded into the life sciences platforms as well. So – and quite honestly, the size of this business is pretty typical for a highly specialized technology of this type. It's kind of an ideal unit of measure, if you will. So, think of it as the puzzle piece of technology that goes well with other pieces that we have.

And honestly, the three primary segments here, we attack from a whole bunch of different places in IDEX, not all of them just in optics and technology. So, space broadband, super complementary to some other things we've talked about along the way in a great market. The life sciences place – side of it, it's probably intuitive. I mean, we do other coatings here. Their technology is a little bit different. And so, so it fits in in a way that we were – we've been looking for for a while. And then, there's a telecom piece that's involved with 5G roll-out and gain filters and things like that. So, it's the kind of work we know how to do.

The other piece of this is their coating capacity, then when aligned with other pockets of coating capacity we have across IDEX, you can start to think of this as an aggregation and think of how you might move capacity around on what's now becoming quite a bit of mass and a very important job to do. So, it's just really, really nice fit. We've known a lot of the folks associated with businesses like this for a number of years. So, it's right in our universe, proprietary transactions. Super happy to have it here.

Vladimir Bystricky

Analyst, Citigroup Global Markets, Inc.

Q

Great. Thanks for the color.

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

A

Thank you.

Operator: And the next question comes from the line of Jeff Sprague with Vertical Research. Please proceed with your question.

Jeffrey Todd Sprague

Analyst, Vertical Research Partners LLC

Q

Hey. Thanks. Good morning, everyone.

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Hi, Jeff.

A

Jeffrey Todd Sprague

Analyst, Vertical Research Partners LLC

I just wanted to come back to Nexsight and KZ. I think you responded to a prior question that they're strong. They look amazingly strong, right? I think an 11 point impact in FMT were acquisition impact in the quarter. Was there something unusual going on or some reclassification or something to drive that big of a result in those businesses?

Q

William K. Grogan

Senior Vice President & Chief Financial Officer, IDEX Corp.

No. I mean, the only thing of note, it was small. It was a couple of million dollars. Just as we got Nexsight on our normal accounting procedure, they picked up a couple weeks incremental revenue. But it was \$2 million, \$3 million type of deal.

A

Jeffrey Todd Sprague

Analyst, Vertical Research Partners LLC

Okay, great. I think I'll leave it there. My other questions were answered. Thank you.

Q

William K. Grogan

Senior Vice President & Chief Financial Officer, IDEX Corp.

Okay.

A

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Sure.

A

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

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Matt?

A

Operator: Matt, your line is now live. You may ask your question.

Will Jellison

Analyst, D.A. Davidson & Co.

Good morning. This is Will Jellison on for Matt Summerville.

Q

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

A

Hello.

Will Jellison

Analyst, D.A. Davidson & Co.

I wanted to learn a little bit more about price and maybe start out with some historical context for how much price was realized in 2022 and how much incremental realization is expected across your businesses in 2023.

William K. Grogan

Senior Vice President & Chief Financial Officer, IDEX Corp.

Yeah, sure. So, price is a big part of our value capture across our portfolio, balancing, hey, we have differentiated products and making sure we capture that value from our customers. Obviously, last year, from an inflationary perspective, we were hitting all-time high. So, we had ramped our price pretty significantly as we went through, I think, topping off close to 5% last year. This year, we guided about 4%. We're on track for that. That's a combination of new price increases that we've launched here throughout the first quarter and then carry-over pricing from actions we took throughout last year.

Will Jellison

Analyst, D.A. Davidson & Co.

That's great. Thank you. And then, as a follow-up, I wanted to get an update on Muon. What is the expectation for organic growth in that business for 2023 and about how much adjusted EPS contribution it's contributing to the guide for the year?

William K. Grogan

Senior Vice President & Chief Financial Officer, IDEX Corp.

Sure. I mean, we haven't disclosed exactly other than it'll be at the high-end of HST growth on a normalized basis. Before we bought them, they had been a double-digit compounder. So, really successful with their growth trajectory historically. And we continue to see that here as they progress in the high single-digits. From an EPS perspective, I'd refer you to our annual guide. We didn't break out the individual pieces. But I think incrementally this year, we said \$0.43 for Muon, the carry-over for Nexsight and KZ, net of the divestiture of Knight.

Will Jellison

Analyst, D.A. Davidson & Co.

Great. Thank you very much.

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

Brett Linzey

Analyst, Mizuho Securities USA LLC

Hi. Good morning, all. Hey, I wanted to come back to HST. So, orders down 23%. Are you able to parse out how much of that decline was specific to the OEM destock versus maybe some softening in other areas of the portfolio?

William K. Grogan

Senior Vice President & Chief Financial Officer, IDEX Corp.

Hey, Brett. I apologize. Can you repeat that question? [ph] It broke up on our side (00:41:24).

Brett Linzey

Analyst, Mizuho Securities USA LLC

Yeah, sure. So, first one is on HST. So, orders down 23%. Wondering if you're able to parse out how much of that decline was specific to the OEM destock versus softening in other areas of that business.

William K. Grogan

Senior Vice President & Chief Financial Officer, IDEX Corp.

[indiscernible] (00:41:45-00:42:04) \$20 million on the one-time order or the blanket order we received last year. So, that was a couple percent of the 23%. The balance is a lot of the market factors that Eric highlighted.

Brett Linzey

Analyst, Mizuho Securities USA LLC

Okay. Got it. And just one other one. You talked about some of the barometer businesses pulling back a little bit. How does that shape your thinking around incremental restructuring or further curtailment of some of this discretionary? Do you lean into the additional actions here to defend the margins? Just curious what the business planning assumption is.

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Yeah. Look, I think so far, it's very much in line with what we had laid out [ph] in our – for the year, (00:42:45) the planning for it. So, remember, [indiscernible] (00:42:49) softening in the back half on the industrial side. We're saying here, this might be some early indications that it will come to fruition. And so, in those businesses, we've already made and lined up the discretionary cost reductions and some thought and care around any additions we might make in a way that's completely in line with what we had originally said.

The targeted actions that we spoke about related to the HST destocking phenomenon, those are pretty targeted actions within those businesses. So, this is where the, if you will, the portfolio nature of IDEX really helps us. We can treat these in kind of a differentiated way, and occasionally, come together on just smart investments around travel and other discretionary things and just do it well as a team.

Brett Linzey

Analyst, Mizuho Securities USA LLC

All right. Got it. Thanks a lot for the color.

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Appreciate it.

Operator: And the next question comes from the line of Joe Giordano with TD Cowen. Please proceed with your question. Hello, Joe. Your line is live. Please ask your question.

Joseph Giordano

Analyst, TD Cowen

Hey. Sorry, I had muted myself. Can you guys hear me?

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Yeah.

A

Joseph Giordano

Analyst, TD Cowen

Okay, cool. So, Nathan had talked about this in his question, but I wanted to follow up there on the inventory thing in HST. And yes, you guys are not typically like components that are overstocked at an OEM. So, just was this a change in behavior like where OEMs just acted differently because – like unbeknownst to you, where they were just buying in excess of their need for a long time and maybe – like maybe that level of granularity is not clear to IDEX? And so, that's one. And then, you guys are generally a company that learns pretty quickly. So, what do you differently coming out of this? Do discussions have to change or how do you kind of make sure that something like this doesn't catch you off guard again?

Q

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Yeah. No, it's a good question. I mean, like if you kind of get it right down to the way that inventory replenishment is done, obviously, your future projections and your assumptions around lead time drive almost all of your requirements. And so, in hindsight, now you can view this and think, well, there must have been irrationality there. But I don't think that's actually the case. I think if you're projecting a line a certain way and [ph] you've generally been (00:45:08) experiencing delivery patterns, not just for us, but for others of a certain level, it's going to say you need a lot of stuff.

A

I think part of what's changed here and maybe changed most dramatically is you had kind of a simultaneous – well, first of all, the calendar change. As funny it sounds, that always tends to bring a different headset. And I think are some legitimate things out there kind of from a macro perspective that people are wondering about. We're further away from COVID. We're starting to see some pullback in biopharma spending. We have some funding crisis associated with start-ups and things in biopharma places. So, the minute you interject that back into the equation, you potentially go change your assumption on long-term demand. It actually has a pretty striking effect on what you should be bringing in.

Now, you combine that with the fact that – we execute really well. So, our lead times and our customer set returning quickly back to normal, you put those two things together, even an automated system is going to say, hey, you've probably got too much here. So, back to your point on learnings and things like that, first of all, we're not typically seeing cycles of this magnitude, these kind of swings. But to be fair, maybe in the world to come, as we see – there seems like there's always another chapter around the corner.

So, I do take your point. And I think higher iteration, really coming together and understanding long-term projections being – maybe we're potentially more transparent with where we are in terms of lead time performance, customer set, making sure that that's exactly understood, not just today, but tomorrow as we move through cycles and swings like this. I think those would be the kind of things that our teams are talking about at both the commercial and the operational level.

Joseph Giordano

Analyst, TD Cowen

No, that's fair. And then, just like last for me on the FMT side. I mean, you talked about April weakening, and I know that your guidance assumes that industrials get worse in the back half of the year. But is the April

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weakening here kind of like in line in terms of magnitude with what you're contemplating at this point, like nothing is – did you expect it to start now? Like how consistent is what you're seeing with what you previously got?

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

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Yeah. I mean, I think this is about the pattern that you would expect at some point. I would say like this is pretty recent. April, as I said, is often a kind of an interesting month of transition as you move into the spring. So, we'll see. But we're always looking for a slight step-down one way or the other and then uniformity, because I think that's where, again, the portfolio nature of IDEX comes into play. We're able to kind of see it across a variety of end markets simultaneously, all of which have kind of the same sort of short order fulfillment patterns that have long been known to people.

So, when they tend to move in concert with each other, either positively or negatively, it's at least worth looking at and taking a signal. I would say this is a small drop. It is uniform in nature. But that is exactly what we would have probably expected and I think is modeled in ultimately in the back-end. And we'll obviously continue to monitor it and talk to you and others about it as we roll through and finish the second quarter.

Joseph Giordano

Analyst, TD Cowen

Q

Great. Thank you, guys.

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

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Thank you.

Operator: There are no further questions at this time. And I would like to turn the floor back over to management for any closing comments.

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Hey. Thanks so much. I apologize. I know we've had some glitches with the technology. Maybe we'll need to put more filters to work on telecommunications. First of all, I want to thank the IDEX employees. I know there's always some listening in on the call. Very, very strong quarter. You've continued to really perform for the business and for our customers. Thanks to others on the call for your interest and support in the company.

Bottom line here, we knew 2023 was going to be a year of recalibration, moving from one state of the world to another. It's playing out more dynamically than we initially suspected in the HST side. But as you can see, we're executing through it. We're taking the appropriate responses in the business. And I think most importantly, we ultimately believe in the long-term success and outgrowth in those markets. We're talking about coming down from highs to something that's actually pretty typical, but absolutely advantaged. We think it's going to continue that way and accelerate for years to come.

So, through all of these dynamic swings of the last three years, I'm really proud of the fact that we've executed well, and we certainly stepped up our capital deployment. Really happy to announce the sixth transaction since the beginning of 2021 with Iridian, doubled our emerging markets footprint and capability set, and continue to strengthen a really unique culture as we've done it. So, we're built for the long-haul here. We're confident that

we're going to perform and deliver value throughout, and I look forward to updating everybody along the way as the year and the – year to come and the years in the future play out for IDEX. Thank you.

Operator: This concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation, and have a great day.

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