24-Apr-2024

IDEX Corp. (IEX)

Q1 2024 Earnings Call

Copyright © 2001-2024 FactSet CallStreet, LLC

CORPORATE PARTICIPANTS

Wendy Palacios
Vice President-FP&A and Investor Relations, IDEX Corp.

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

Abhishek Khandelwal
Chief Financial Officer & Senior Vice President, IDEX Corp.

OTHER PARTICIPANTS

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

Deane Dray
Analyst, RBC Capital Markets LLC

Vladimir Bystricky
Analyst, Citigroup Global Markets, Inc.

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

Joseph Giordano
Analyst, TD Cowen

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

Rob Wertheimer
Analyst, Melius Research LLC

MANAGEMENT DISCUSSION SECTION

Operator: Greetings and welcome to the IDEX Corporation First Quarter 2024 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 Wendy Palacios, Vice President-FP&A and Investor Relations. Thank you. You may begin.

Wendy Palacios

Vice President-FP&A and Investor Relations, IDEX Corp.

Good morning, everyone. This is Wendy Palacios, Vice President of FP&A and Investor Relations for IDEX Corporation. Thank you for joining us for our discussion of the IDEX first quarter 2024 financial highlights. Last night, we issued a press release outlining our company's financial and operating performance for the three months ending March 31, 2024. The press release, along with the presentation slides to be used during today's webcast, can be accessed on our company website at www.idexcorp.com.

Joining me today are Eric Ashleman, our Chief Executive Officer and President; and Abhi Khandelwal, our Senior Vice President and Chief Financial Officer. Following our prepared remarks, we will open the call up for your questions. If you should need to exit the call for any reason, you may access a complete replay, beginning approximately 2 hours after the call concludes by dialing the toll free number 877-660-6853 and entering conference ID number 13742103, or simply log on to our company homepage for the webcast replay.

Copyright © 2001-2024 FactSet CallStreet, LLC

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 an IDEX filing with the Securities and Exchange Commission.

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

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Thanks, Wendy, and good morning, everyone. I'm on slide 3. In Q1, our core execution capabilities delivered strong results, particularly within our Fluid & Metering Technologies and Fire & Safety/Diversified Products businesses. We experienced an encouraging lift in sequential orders from our core industrial and municipal markets after a period of elongated destocking. And we were able to quickly capitalize on this bounce and deliver for our customers. Our lead times and overall responsiveness are at outstanding levels as we stripped out excess inventory and improved overall productivity. Our closest to consumption businesses within FMT pulled back a bit in March after a strong January and February launch, but things stabilized again in early April, suggesting our initial take on overall modest support for 2024 remains the correct call.

The Health & Science Technologies segment performed to expectations, but there are puts and takes there as we consider individual recovery rates within our markets and application sets. Our tactical priorities favor those growth initiatives that best leverage our most differentiated technologies in line with markets showing higher probabilities of near-term inflection. Largely through inorganic efforts, we've expanded our technical capabilities within HST to support the highest quality semiconductor technologies to power the AI revolution. We have increased content within the transformative world of low-orbit space broadband. We are increasingly called upon to help companies develop and deploy advanced technologies for national defense. And we have ambitions to continue to add to these capabilities as we further leverage our balance sheet through M&A.

We continue to watch for signs of recovery in life sciences and analytical instrumentation and are ready to capitalize on growth at the first signs of improving customer demand. Our businesses serving these spaces are exceptionally well-positioned with highly credible expertise. We have confidence in our ability to outperform again once this market correction runs its course.

Overall, it's clear that economic and geopolitical uncertainty persist as a backdrop for all companies. We've leaned into that with a conviction that the three core tenets of the IDEX difference and expression of our most basic differentiated mindset help us play offense. Our great teams and talent work together and superior businesses with a special culture. We practice 80/20 to align around the few things that really matter, and we leverage natural proximity to the customer to solve their toughest problems quickly to support our outstanding economics.

We ultimately create compounding value for shareholders by driving organic growth outperformance through our top growth bets. We amplify these bets through acquisition of complementary, faster growing companies, and we expand margins and generate strong free cash along the way as our leaders apply the five core tools of the IDEX operating model. I'd like to thank our IDEX teams around the globe for their dedication to these principles and for delivering strong performance in Q1.

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

Copyright © 2001-2024 FactSet CallStreet, LLC

Abhishek Khandelwal

Chief Financial Officer & Senior Vice President, IDEX Corp.

Thanks, Eric. Before jumping into the consolidated results on slide 4, I want to highlight our team's consistent ability to execute as is seen in the results, delivering strong profitability and free cash flow in the first quarter, despite challenging year-over-year comparables. Moving on to the consolidated financial results. All comparisons are against the prior year period unless stated otherwise.

Orders of $820 million in the first quarter were down both 1% overall and organically. We experienced an organic decrease in FMT and HST, while FSDP grew low double-digits, driven by strength in dispensing and emerging markets. First quarter sales of $801 million were down 5% overall and down 6% organically. We experienced a 13% organic decrease in HST and a 3% organic decrease in FMT, while FSDP grew by 2% organically.

First quarter gross margin was 44.6%, declining 60 basis points, while adjusted gross margin was 45%, contracting 20 basis points due to lower volume leverage, partially offset by price cost and operational productivity. First quarter adjusted EBITDA margin was 26%, down 120 basis points. This is a sequential improvement versus fourth quarter of 20 basis points as we remain focused on margin expansion. I will discuss the drivers of first quarter adjusted EBITDA on the next slide.

On a GAAP basis, our Q1 effective tax rate of 21.5% versus last year's first quarter effective tax rate of 22.2% decreased primarily due to a favorable discrete item. First quarter net income was $121 million, generating EPS of $1.60. Adjusted net income was $143 million, with adjusted EPS of $1.88, down $0.21 from the prior year first quarter.

Finally, free cash flow for the quarter was $137 million, up 13% over the prior year period. We achieved a conversion rate of 95% of adjusted net income, mainly driven by lower variable compensation payments and capital expenditures, despite lower adjusted net income. On an organic basis, we drove more than $78 million of inventory reduction over the last 12 months and we saw inventory turns improve 0.4 turns year-over-year.

Slide 5. Moving on to slide 5, which details the driver of our first quarter adjusted EBITDA. For the first quarter, adjusted EBITDA decreased by $22 million, compared to the first quarter 2023. Our 6% organic sales reduction unfavorably impacted adjusted EBITDA by $29 million, flowing through at a prior year adjusted gross margin rate. Price cost was accretive to margins and we drove operational productivity that offset employee-related inflation. These results yielded in a negative 50% organic flow-through. The impact of FX and acquisitions, net of divestitures, contributed $3 million of adjusted EBITDA in the quarter, resulting in a negative 48% flow-through.

With that, I'll provide a deeper look at our segment performance. I'm on slide 6, within our FMT segment. In our water businesses, municipal project activity remained strong. Note that water sales performance in first quarter of the prior year was favorably impacted by both hurricane-related backlog execution and the catch-up of a one month lag treatment of the Nexsight acquisition, effectively recording four months of Nexsight sales in the first quarter of 2023. Our energy businesses remained stable with favorable infrastructure tailwinds, offset by a mild winter. Our agricultural businesses continue to be cyclically down in line with expectations. Finally, Q1 adjusted EBITDA margins expanded 60 basis points, driven by price cost and operational productivity, despite slightly lower volumes.

Moving on to page 7. Despite challenging year-over-year comparables, the Health & Science Technologies segment performed to expectations and nearly all of our adjusted business saw sequential orders improvement as compared to the fourth quarter. Our teams continue focusing on our more strategic customers, next-gen solutions in life sciences and analytical instrumentation, while we watch for signs of recovery. Our space,

Copyright © 2001-2024 FactSet CallStreet, LLC

broadband, and laser communication initiatives continue on track, despite current quarter customer delays. Our material processing technology business saw strength in food and sports nutrition that offset conservative customer capital investments within biopharma and pharma.

For semiconductor, we saw orders improvement up both year-over-year and compared to the fourth quarter. And we expect these trends to continue in line with an improved outlook for memory chips. In line with our FMT industrial businesses, [ph] that's just the industrials are steady (00:10:44). Lastly, adjusted EBITDA margins improved 40 basis points over the fourth quarter of last year. A year-over-year decline of 250 basis points was driven by volume leverage, partially offset by price cost and operational productivity.

Now, turning to slide 8. Our Fire & Safety/Diversified Products segment performance was driven by dispensing project wins in emerging markets, which helped offset the impact of key US customers' multiyear refreshment cycle. We continue to see stability in Fire & Safety. In the quarter, our focus on strategic share gain initiatives helped partially offset unfavorable budget reallocations in the industry. BAND-IT automotive demand is strong with growth expected in the year. Additionally, industrial performance was similar to FMT and HST with sequential improvement versus Q4. Finally, adjusted EBITDA margins expanded 40 basis points driven by price cost.

With that, I'd like to provide an update on our outlook for the second quarter. I'm on slide 9. In Q2, we're projecting GAAP EPS to range from $1.75 to $1.80 and adjusted EPS to range from $2 to $2.05 with organic revenue decline of approximately 2% to 3% and adjusted EBITDA margin of approximately 27.5%. Turning to the full year 2024. We're maintaining our previously issued full year outlook of organic revenue growth of 0% to 2% and adjusted EBITDA margin of approximately 28% and adjusted EPS of $8.15 to $8.45, with majority of markets performing in line with our initial guidance and our focused efforts on driving growth bets.

With that, I'll turn it over to Eric for his closing remarks.

Eric D. Ashleman

President, Chief Executive Officer & Director, IDEX Corp.

Thanks, Abhi. I'm on slide 10 . I'd like to close by coming back to the simple value equation I talked about in my opening remarks. It all starts with organic growth outperformance, typically targeting 300 basis points above market entitlements. We drive about 20 to 25 bets across the company at any one time to achieve these results. I highlighted earlier some examples of growth initiatives through applied technologies within HST. Within FMT, we're also working on integrating the recently acquired assets within our Intelligent Water Group, alongside our legacy technologies to support critical analytical work within municipal and industrial wastewater containment and processing. Also within FMT, we're deploying digital tools across multiple brands that go-to-market through distribution to enhance our customer experience and promote share gain. I'll go deeper in the quarters ahead with additional specific examples to help bring this work to life.

We amplify these bets with complementary and organic work via M&A to add another 200 to 300 basis points of growth. We see an outstanding opportunity to support faster growing transformational markets through the disciplined build of relative and absolute scale within very high-quality niches. Over the last three years, we've been working this play in the Intelligent Water space, within thin film optics and within the niche of small form factor materials intensive processing. Finally, we expand margins and seek to drive double-digit earnings growth along the way as our teams deploy the five basic IDEX operating model tools, with 80/20 as our heartbeat. Our decentralized environment and collaborative culture supports speed and agility and our inclination to resist top heavy infrastructure supports financial leverage as we grow.

Copyright © 2001-2024 FactSet CallStreet, LLC

In closing, the world is transforming and evolving in exciting but unpredictable ways. We're building a company that thrive and win in that environment, where power meets speed and agility at the intersection of technology and culture. I look forward to communicating our progress with you along the way.

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

QUESTION AND ANSWER SECTION

Operator: Thank you. Ladies and gentlemen, at this time, we will be conducting a question-and-answer session. [Operator Instructions] Our first question comes from the line of Mike Halloran with Robert W. Baird. Please proceed with your question.

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

Q

Thanks. Good morning, everyone.

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

A

Good morning, Mike.

Abhishek Khandelwal
Chief Financial Officer & Senior Vice President, IDEX Corp.

A

Good morning, Mike.

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

Q

So just a simple question, Eric. Maybe just talk about in your mind if anything's really changed in the market since you gave the last guidance or from an expectation perspective. Obviously, dispensing a little better in the first quarter doesn't seem like your expectations for the remainder of the year are all that different. But when you go through some of the key end markets, has much really changed from an outlook perspective and how are you thinking about the sequentials through the year versus normal seasonality, ignoring some of the self – the positive things that you are driving with some of your investments?

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

A

Yeah. No, thanks for the question. I mean, not a lot is different. I mean, I provided some color around the cadence of those kind of smaller flow FMT order of businesses that we have that are such good diagnostics. I think just to show that at the end of the day that the call remains the same. But it was interesting to watch the sensitivity kind of ebb and flow in a way. It's a little unusual, hot January and February, a little bit of pullback in March, kind of coming back to equilibrium in April. So I think that's interesting mainly because I think it's reflective of the, frankly, the level of sensitivity that is out there as people track inflation, interest rates, election. But I think we still land at the same place.

When we look at particularly the markets in HST, of course, about half of it is pretty industrial too, so it kind of follows that same rhythm and cadence. I think what we see is shoots of growth kind of around the periphery of the

Copyright © 2001-2024 FactSet CallStreet, LLC

larger pieces of HST. So our MPT business got some great things going on in terms of food production or battery material handling, but not necessarily in the core pharma. That's still to come. We saw a little lift in feeling around some – kind of coming off the bottom in consignment orders, largely in that kind of memory chip world. But we still await the broader lift on the highest quality semicon offerings that we have in the company.

So when you step back, I think, kind of broad but modest support on much of the industrial landscape of IDEX. And then I think a lot of attention for us back on those kind of two core higher growth potential markets within HST of life science and analytical instrumentation and the semicon markets and kind of great 2025 sitting there. And it's just a question of how much in the back half do you start to see some velocity towards it. And that's pretty close to where we were, I think, three months ago.

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

Q

Yeah. No, makes sense. And then an HST margin question, obviously, you're running well below peak right now. When you get mix normalized and those end markets come back, whether it's 2025 or later, that part of this year as you just mentioned, how do you think about margin normalization? Is that 25% to 27% kind of range you add towards peak? Is that still the bogey for where you think things will be when you get a little more normalization and maybe just put a little context around that because there have been some moving pieces to that segment?

Abhishek Khandelwal
Chief Financial Officer & Senior Vice President, IDEX Corp.

A

Yeah. Mike, this is Abhi. So I think if you go back 90 days and think about the discussion we had at the end of Q4, I think, look, what we've said is as the volumes come back in HST, more specifically in life science and the semicon piece that Eric just talked about, this business levers really well. And what we have said is we expect margins to be closer to 30% in HST once our volumes are back. Hey, Mike.

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

Q

Yeah. Sorry. I just assumed the operator was going to cut me off. So 30% EBITDA margins when everything comes back [ph] okay because the (00:19:08) 25% to 27%, just for clarity, was me just looking at previous margin ranges. So, okay, that makes sense. That makes sense. Really appreciate it, everyone.

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

Deane Dray
Analyst, RBC Capital Markets LLC

Q

Thank you. Good morning, everyone. And a special welcome to Wendy and congrats on the new role.

Wendy Palacios
Vice President-FP&A and Investor Relations, IDEX Corp.

A

Thank you, Deane.

Deane Dray
Analyst, RBC Capital Markets LLC

Q

Copyright © 2001-2024 FactSet CallStreet, LLC

Hey, Eric, I think you've given some of the color here, but just regarding your read on how the year is beginning to play out, can you also touch on day rates? And it sounded like BAND-IT started off well.

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

A

Yeah.

Deane Dray
Analyst, RBC Capital Markets LLC

Q

So that's always a good sign. And anything else about the bellwethers, Warren Rupp, and some of the others?

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

A

Yeah. And that cadence that I articulated in the opening, in Mike's question was really right there. It was on those bellwether businesses that we aggregate, take a look at weekly, and then kind of used as an ultimate barometer of industrial health for IDEX. And I think again, we saw those launching really strong in January, continued into February. It was interesting, a little bit of a pullback in March, and we had Easter earlier than ever before. So it's probably some of it. But to kind of see that swing and see it as broadly too, certainly caught our attention and yet then it sort of stabilized again in April. So it's moving a little faster. Both directions than it typically has. And yet the arrow still remains kind of at the exact same slope that we thought.

I just want to point it out because, again, I think it's reflective of some of the dialogue and conversations we're having. And this is higher up the food chain around projects, confidence, where we are. It does seem more sensitive than I've seen it in a long time to kind of whatever's on the news and what's out there, which isn't really surprising given kind of what this year is and where we are. So largely an unchanged position, but I thought the color might be helpful.

Abhishek Khandelwal
Chief Financial Officer & Senior Vice President, IDEX Corp.

A

And just to build on it, I think the other thing it points to, that we've had a lot of conversations around is this normalization of the supply chain. So it's a lot faster when it turns on, a lot faster when it turns on because people know that the lead times are back to normal levels, that they can adjust their demand as they see the markets move up and down.

Deane Dray
Analyst, RBC Capital Markets LLC

Q

That's real helpful. And I'm glad you mentioned about that normalization of supply chain because that's been a focus. And just separate question on the life sciences, analytical instruments market. We've been watching this and just kind of waiting where and how that the destocking might run its course and it just really hasn't turned the corner yet. I did see one of the life science guys report a strong quarter, but that was more on the bioprocessing side, less on the instrument side. But what's the typical lag between what you see from the OEs in terms of their sales of instruments versus your supply of these components? I mean, I guess some of it has to do what their inventory levels are and whether they're running off their current stock and then whether they're pulling from – to you for their orders. But just the typical lag and any color there would be helpful.

Copyright © 2001-2024 FactSet CallStreet, LLC

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

Yeah. Well, so I think there's a couple of points to hit there. I'll start with the first where you ended. I mean, the lag is – I mean, it's not extended for us because most of our replenish cycles and lead time fulfillment abilities and capabilities of components going to companies like that is really fast. I mean, it's one of the reasons that when this sort of destocking cycle started, we were one of the first to come and recognize it back in Q4 of 2022. And so I think any sign of life, we're going to see that first. And we're going to see it probably pretty close to the time that they're talking about selling the instruments just because of the natural way that forecast would roll in and come back into our factories. Typically, and I'll – this is for most cases, I mean we're not requiring months and quarters of heads up on that just because we're set up to quick turn most of the components.

I think maybe the only exception would be, look, if there's a material shift in the overall demand profile, then we've got to think about making sure that we get those same broader signals out to our suppliers, and they do that with us. You have to have that conversation, but sort of the early turn and inflection would be relatively quickly aligned. The only other point kind of embedded in the earlier part of your question to come back to is, just as we're all reading signals from the broader market as you're thinking of IDEX, it's always important to recognize we participate in the instrument side of those sales. And often, you'll see people are talking about consumable streams and maybe those would tend to advance and start to move ahead of instruments. And so it's an interesting point, but you always have to kind of equate it back to and what's the velocity on instruments because ultimately that's where the components that we supply go.

Deane Dray
Analyst, RBC Capital Markets LLC
Q

That's really helpful. Thank you.

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

Thanks, Deane.

Abhishek Khandelwal
Chief Financial Officer & Senior Vice President, IDEX Corp.
A

Thanks, Deane.

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

Hey, good morning, everyone.

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

Hey, Vlad.

Copyright © 2001-2024 FactSet CallStreet, LLC

Vladimir Bystricky
Analyst, Citigroup Global Markets, Inc.

Q

Thanks for taking my question. I guess, can you just talk about, and sorry if I missed it, what price versus cost overall actually was in the quarter? And your expectations for price versus cost for the year and what you're seeing in terms of inflationary pressures versus your expectations coming into the year?

Abhishek Khandelwal
Chief Financial Officer & Senior Vice President, IDEX Corp.

A

Yeah, Vlad, this is Abhi. I'm more than happy to answer that for you. So, if you recall when we talked about our Q4 earnings, what we talked about was price for 2024. We'd laid it out at about 2%. But more importantly, what we were focused on was this price cost spread of 80 to 100 basis points. So as you think about where we exited Q1, we were closer to that 100% from a price cost standpoint in line with expectations, in fact, on the high end of expectations. If you go back in time, you can just look at IDEX historically. We've seen from a pricing standpoint is something in the neighborhood of 0.8% to 1.2%. So this pricing that we have laid out for 2024 is higher than normal levels. And then the price cost spread typically what we've seen historically is 30 to 40 bps versus what we're seeing here, which is 80 to 200 bps. To answer your second question on inflation, what we're seeing is the input costs slightly favorable compared to what we assumed in the guide that we had laid out as part of the Q4 discussion.

Vladimir Bystricky
Analyst, Citigroup Global Markets, Inc.

Q

Great. That's helpful color, Abhi. Appreciate it. And then just to go back to HST, in terms of the organic sales decline that we've seen in the quarter, are you able to give us more color on the underlying growth rates in industrial and semicon versus what you're seeing in life sciences and analytical instrumentation?

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

A

Well, a couple of things there. I mean, the comparisons in a lot of HST are pretty exaggerated levels, given the rapid destocking that we saw last year. And so we've been talking about life science and analytical instrumentation as being in a general condition of kind of flat waiting for signs of recovery. And that, just from a segment percentage, it's just over a third of the entire segment. I think semicon certainly has high single-digit growth potential, and we're starting to see some early signs. I mentioned some things in sealing and a couple of other places. We really have a little bit more of that dialed in in the back half as we start to kind of approach that entitlement. It's probably 2025 though before it really comes in at that full level. I think the industrial space we kind of talked about it, it tracks with generally what we're saying about FMT and much of FSDP overall, so it's more modest in the low single-digit range right now.

And I don't know, Abhi, if you want to add something there.

Abhishek Khandelwal
Chief Financial Officer & Senior Vice President, IDEX Corp.

A

Yeah. No, the only thing I'd add is I think just – look, we've talked about this. I think comparing it year-over-year is kind of tricky given what we saw last year. So I think it's important to kind of point out, if I look at the sequential order trends and look at the sequential order patterns from Q4 to Q1, we saw about $59 million of order uptick. $14 million of that was tied to HST, half of that I'd say is blanket with our large customers that give us blanket that we ship throughout 2024. The other half is normal book-to-bill. You look at FMT, we're up about $28 million in orders sequentially. Again, half true demand that we've talked about tied to our bellwether businesses and the

Copyright © 2001-2024 FactSet CallStreet, LLC

other half being blanket. And lastly, FSDP is the story around emerging markets and the growth coming out of India. That's really exciting for us. So you saw that sequentially. So again, I think the key here – the focus here is to look at it sequentially, because I think that's a better way to look at the business given where we are in the cycle.

Vladimir Bystricky
Analyst, Citigroup Global Markets, Inc.

Q

Okay. That was really helpful, guys. Thanks. I'll get back in queue.

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.

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

A

Hey, Nathan.

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

Q

Getting back on to the HST order patterns and the sequential improvement that you've seen there. It's obviously up quite a lot off the bottom from third quarter 2023. Customers did a lot of inventory destocking out of some of those businesses. Is it your view that customer inventories have been rightsized and we're kind of moving back to an area where your orders are pretty close to what your end customers are selling? Or is it still continued destocking going on from your customers and do you have visibility into that?

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

A

Well, so I kind of break down HST because I think the answer varies a bit depending on the portionality of the pieces. So half of it is broadly industrial, again, more like FMT and the rest of IDEX. And I think there, like in those other areas, I'd say the destocking trends are largely past us. And so part of that lift you're seeing in that industrial core and it's because frankly we're at about the levels of consumption. And as those become more positive, we rise with them. So you see the same dynamic in about half of HST that you see elsewhere.

I think in the other areas, it's a little trickier. And the visibility, to be fair, is a little bit murkier because of just the extension of those supply chains. So now, in life science and analytical instrumentation, of course, we can best see inventory between us and factories. And ultimately, that cleared very fast for us so I don't see an inventory accumulation there. End devices, which of course have global reach, harder for us to see. We ask about it all the time and there probably are pockets here and there of different platforms and things that are out there that we're probably still working through. So I'd say there may be some moderate or minor effects there, but they're just harder to see and they're kind of outside the four walls of where our usual experience is.

And then in semicon, I think it varies as well because there's such discrete and different pieces of semicon. So things associated with memory, as I said, for us, that's kind of simple consignment stock and it's starting to move

Copyright © 2001-2024 FactSet CallStreet, LLC

off the bottom, which would indicate, okay, we cleared that inventory too. Some of the kind of higher tech things at the other end of the spectrum, more anchored towards high end lithography or metrology, I think quite honestly, we're just waiting – the entire industry is waiting for a stronger demand catalyst there to get it moving. So figure, half of the segment, generally clear, looks a lot like industrial IDEX. And then I'd say kind of 50/50 in the other half, depending on these two large pieces.

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

Q

That's helpful. Thanks. Maybe [ph] I'm back on to (00:31:34) the margin question and where it gets back to in a more normalized volume environment. I think you said 30%. First, is that an EBITDA margin target? Because historically, we'd been talking about operating margins.

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

A

EBITDA margin, Nathan.

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

Q

Yeah, thanks. And I would think that during this downturn, that that business carries a lot of very highly skilled labor that you would be really hesitant to rationalize during a downturn, particularly one that's likely to be short and cyclical. And so that's led to some of these pretty high decrementals that you're seeing in that segment, that should also result in very good operating leverage and very high incrementals as we come out the other side. So any commentary you can give us on kind of what you'd expect to see out of incremental margins in HST as we see that volume [ph] adjust (00:32:26)?

Abhishek Khandelwal
Chief Financial Officer & Senior Vice President, IDEX Corp.

A

Well, Nathan, I think the point you made is the answer. But I will say it, which is to your point, we've been very, very thoughtful in terms of how we rightsize the business. Again, as Eric talked about the long-term vision, we believe in the long-term vision of the business and expect this business to grow as we come out of this cycle. So as you think about the incrementals on the uptick, I said 35% to 40% is the incrementals you should expect if not north of it, depending on the investments we make in the business over the long-term as we grow this business.

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

Q

Thanks very much for taking my questions.

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

A

Thanks, Nate.

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

Joseph Giordano
Analyst, TD Cowen

Q

Copyright © 2001-2024 FactSet CallStreet, LLC

Hi, guys, good morning.

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

A

Hi, Joe.

Abhishek Khandelwal
Chief Financial Officer & Senior Vice President, IDEX Corp.

A

Good morning, Joe.

Joseph Giordano
Analyst, TD Cowen

Q

Just curious, like on the tools and the life science piece of HST, is there – like medium-term, is there any sort of like adjustments to the top end of like what this potential is? I mean, I know we're going to get to the end of the destocking, all that over the next – this year and long-term. There's a clear call, but like as – do we need to like adjust what we think like the potential is over like a multiyear period here given what's happening internationally and things like that?

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

A

All right. I think there's probably a couple of things out there to consider at the highest level when you're projecting. I think you hit one of them. So the ultimate position of China in this market, I think, is something everybody has to think about. It's a big part of the issue currently because it was such a high catalyst of growth here more recently for most of the customers that we supply. And so kind of where that comes out, there's some regulatory things that are out there in the mix. I haven't seen a big move in this particular area from any stimulus programs that have been applied over there. So kind of where it ultimately settles in I think is an open question.

On the other side though, probably on the positive, and the question would be, does it offset it? We continue to see just massive technology advancements here. I know the things that we're working on with customers in our building certainly have even potentially higher growth potential as you think of where that may land on a global populations and what work that could get done. So kind of I put the nature of innovation as a positive and where it goes and keeping track of it and seeing what it can all do, right next to a question on China is probably the two biggest calls.

Joseph Giordano
Analyst, TD Cowen

Q

Would you say like globally it's longer-term fungible. Like there's a baseline global demand that is going up and whether it's China or elsewhere where this needs to be put in, it needs to be put in. And like it's just friction over like a shorter-term basis. Is that how you kind of think about it?

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

A

I think that's exactly how we would think about it. I mean, it's – the China piece in particular is pronounced from a – just the relative nature of what it had been and what it is now. And that's not trivial. A couple of positive years on the one side and a few adjustment on the other. But long-term, this is ultimately about applying life saving technology, transformational technology, of course, a global population. And I think certainly, one of the things

Copyright © 2001-2024 FactSet CallStreet, LLC

that we always intended with our franchise is having global reach and scale. We have that. So if it begins to shift around and move from one region to another to do the work, that's actually something we're very well set up to align with. So I think that's well stated. Kind of near-term, which way are the winds blowing? I think more medium-term, it's more regionally around some of these key questions. And long-term, it seems very, very assured. And I think it's ultimately about do you have the scale to go chase it and we do.

Joseph Giordano
Analyst, TD Cowen

Q

All right. Thanks, guys.

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

A

Thank you.

Abhishek Khandelwal
Chief Financial Officer & Senior Vice President, 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. Good morning. I wanted maybe just a little bit of commentary and maybe a little bit more granularity on what you're seeing in the M&A pipeline at present, which businesses, which end markets are you focused on, what are you seeing as far as purchase price multiples? Just a little more detailed color there.

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

A

Yeah, well, I think you saw in the remarks that I had, I mean, I made a special point to talk about the fact that we're looking for complementary pieces, so things that attach well to other areas of IDEX. And I mentioned I think in a high level how we had done that over the last three years in the optics space, the water space. And then I called it material intensive processing on small form factor. That's where Muon fits and frankly STC. So these are businesses that when we purchase them, not only are we purchasing a great IDEX like business, but we can see attachment points, more natural synergies. And frankly, it matches the vision of something that we're trying to create there.

Much of which comes back to the question that we just talked about in the life science arena of, can we have the relative and the absolute scale to do that job well as it globalizes? And so I think that the areas that I highlighted here would be – you can take those as areas of high interest and you can see the evidence of things that we've applied there. Valuations, I think we've consistently said for the kind of quality that we look for at IDEX, it remains quite pricey. I will tell you, I think we put in a lot of work here recently where the capital deployed number for us would be higher if we were willing to go a couple more turns and meet some of the expectations. And we just did not. We still are very, very disciplined about what we can do with the business. Even in the case where it's complementary like that, they're just – we know what the limit is and we've held that line and we'll continue to do that.

Copyright © 2001-2024 FactSet CallStreet, LLC

So I think one other aspect I would put it as a net positive for us, we continue to find ourselves in proprietary spaces, having conversations with people generally where it's only the two of us. And so I think that's important in this environment too. That gives you a bit of a head start. But the takeaway here is absolutely urgent. And we're putting the time in, we're putting the effort in. We are narrower in our focus because we are looking for things that attach well and scale quite naturally within these niches. And we're doing it in a proprietary basis, but we are super careful about where the line needs to end on valuation for us.

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

Q

Got it. And then just as a follow-up, could you maybe spend a minute talking about kind of the ultimate duration and strength of the muni water and wastewater cycle as you kind of see it playing out for IDEX? Thank you.

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

A

Yeah, I think as I said a couple of times before, I don't think it launches with a lightning bolt or a bang. But actually, the duration of it is going to be very durable. You've had a lot of intentional funding announcements put out there. Those always take a while to find their way home and funded projects that have been engineered and are now being deployed. So I think what's very positive about this cycle is the – and I can't think of another one where I've seen this much intentional focus. And frankly, this much unfortunate reinforcement in terms of things in systems that are just not able to cope with the current climate that we have out there. So you put those two things together and what we know is that level of confidence is what it really takes for engineers and municipalities and industrial spaces to do the work, to make it through the budget cycles, the inevitable number of conversations to get things approved to get them in front of us.

The last point I always remind external folks to consider when they think of our water businesses, a lot of what we're doing is analysis. So we're doing infrastructure analysis and then providing that over generally for a technical part of our customer set. And so in that way, we're actually well-positioned to kind of as a diagnostic at the beginning of the cycle because much of the time they're using our information and our output to substantiate larger capital projects. And so kind of here in the beginnings of a multiyear cycle is a good place for IDEX to be because we're actually helping them put the projects together that's going to extend the cycle overall.

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

Q

Great. Thanks for the color, Eric.

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

A

Thanks.

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

Copyright © 2001-2024 FactSet CallStreet, LLC

Thank you much. Eric, you touched on an interesting topic in your opening comments just on semiconductors and the AI shift, which is obviously driving huge changes in demand, pricing, power, all sorts of things across pockets of industrials. I wonder, do you have any expanded remarks on what your exposure is there, how your technological capabilities are changing, whether you're entering kind of a new segment of semiconductors, anything you can flesh out there if you're willing?

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

Yeah. No, I appreciate it. I mean, it's still a modest portion of IDEX overall, but it's growing and it's growing and has found its way into the portfolios of some of the things we've recently acquired in HST. So we're certainly more interested and focused on it. And as we've brought those technologies in, I mean, we've thought about this revolution and the jobs to do within it, particularly the hardest ones, is our number one area of interest. So we're often going right into lithography instruments and some of the most advanced that are out there because those are the ones that are being called upon to do the work, to create the chip architecture that's going to support the hardest piece of this. So we're well-indexed there. We've long had a metrology portion of our business that's all about validating that that job was done well. Even on the piece within water that we have [ph] that's somewhere semi focused (00:42:45), I mean, it's absolute critical, water purification delivery and heating. And we talked about that in our sustainability report is one of the best eco-friendly solutions we have in the whole company.

And so it's a broad market, it's fragmented and segmented into different uses and technologies. But you can think of us is generally thinking about what are the hardest jobs to do that provide the most critical differentiate – and differentiation when they are done. Because typically for us, that's where the most economic benefit comes from. And so we're tracking a lot of that – those different trends, the size of chips, the way that they're being packaged and looking for all the ways that we can play there. So just think of it is that's how we're indexed, that's increasing, and so ultimately as that plays out, I think we're very, very well-positioned.

Rob Wertheimer
Analyst, Melius Research LLC
Q

Great. I'll think about it. Thank you very much.

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

Thank you.

Operator: There are no further questions in the queue. I'd like to hand the call back to management for closing remarks.

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

Well, thank you very much. Thanks for everybody joining today. We appreciate your interest in IDEX. And look, I think no doubt there are some uncertainties out there in the near-term, whether it's inflation and interest rates, geopolitical tensions. It's obviously an election year. We hear a lot of chatter about that out in the background. As I said, I think there's some sensitivity to it. But more broadly, I still think the arrows are very positive for businesses like ours and others over time. So we're tracking all that. We think it's helpful to provide that color to you as we do it.

Copyright © 2001-2024 FactSet CallStreet, LLC

And as you know, we were very good at moving resource round from here to there within this high-quality portfolio to continue to execute for shareholders and customers. But I really step back and say, I think we're incredibly positioned for where things are going in the long-term. And we've had that discussion here with life science and analytical instrumentation, how powerful that's going to be over time. We just had it here more recently with our discussion around semicon and the revolutionary aspects of AI and the part we play there. And then we could go through a host of other applications, more of the niche than not and take you through that as well. And that's what we're building each and every day through our own organic efforts and the inorganic efforts of the company. And so we're laser focused on the things that matter both short-term and long-term. And look forward to continuing to talk with you along the way in the quarters to come. Have a great day.

Abhishek Khandelwal

Chief Financial Officer & Senior Vice President, IDEX Corp.

Thank you.

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.

Disclaimer
The information herein is based on sources we believe to be reliable but is not guaranteed by us and does not purport to be a complete or error-free statement or summary of the available data. As such, we do not warrant, endorse or guarantee the completeness, accuracy, integrity, or timeliness of the information. You must evaluate, and bear all risks associated with, the use of any information provided hereunder, including any reliance on the accuracy, completeness, safety or usefulness of such information. This information is not intended to be used as the primary basis of investment decisions. It should not be construed as advice designed to meet the particular investment needs of any investor. This report is published solely for information purposes, and is not to be construed as financial or other advice or as an offer to sell or the solicitation of an offer to buy any security in any state where such an offer or solicitation would be illegal. Any information expressed herein on this date is subject to change without notice. Any opinions or assertions contained in this information do not represent the opinions or beliefs of FactSet CallStreet, LLC. FactSet CallStreet, LLC, or one or more of its employees, including the writer of this report, may have a position in any of the securities discussed herein.

THE INFORMATION PROVIDED TO YOU HEREUNDER IS PROVIDED "AS IS," AND TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, FactSet CallStreet, LLC AND ITS LICENSORS, BUSINESS ASSOCIATES AND SUPPLIERS DISCLAIM ALL WARRANTIES WITH RESPECT TO THE SAME, EXPRESS, IMPLIED AND STATUTORY, INCLUDING WITHOUT LIMITATION ANY IMPLIED WARRANTIES OF MERCHANTABILITY, FITNESS FOR A PARTICULAR PURPOSE, ACCURACY, COMPLETENESS, AND NON-INFRINGEMENT. TO THE MAXIMUM EXTENT PERMITTED BY APPLICABLE LAW, NEITHER FACTSET CALLSTREET, LLC NOR ITS OFFICERS, MEMBERS, DIRECTORS, PARTNERS, AFFILIATES, BUSINESS ASSOCIATES, LICENSORS OR SUPPLIERS WILL BE LIABLE FOR ANY INDIRECT, INCIDENTAL, SPECIAL, CONSEQUENTIAL OR PUNITIVE DAMAGES, INCLUDING WITHOUT LIMITATION DAMAGES FOR LOST PROFITS OR REVENUES, GOODWILL, WORK STOPPAGE, SECURITY BREACHES, VIRUSES, COMPUTER FAILURE OR MALFUNCTION, USE, DATA OR OTHER INTANGIBLE LOSSES OR COMMERCIAL DAMAGES, EVEN IF ANY OF SUCH PARTIES IS ADVISED OF THE POSSIBILITY OF SUCH LOSSES, ARISING UNDER OR IN CONNECTION WITH THE INFORMATION PROVIDED HEREIN OR ANY OTHER SUBJECT MATTER HEREOF.

The contents and appearance of this report are Copyrighted FactSet CallStreet, LLC 2024 CallStreet and FactSet CallStreet, LLC are trademarks and service marks of FactSet CallStreet, LLC. All other trademarks mentioned are trademarks of their respective companies. All rights reserved.