1st Quarter 2016 Earnings Conference Call Transcript

May 4, 2016

Overview*:

BDC reported 1Q16 consolidated revenues of $543.8M. On a year-over-year basis, EBITDA margins of 16.4% increased 90 basis points and EPS grew 1% to $1.01. BDC paid down $51 million of debt in the quarter and increased guidance for the full-year 2016. BDC now expects FY16 revenue to be $2.320 - $2.370B and EPS to be $5.15 – $5.45. BDC expects 2Q16 revenue to be $570 - $590M and EPS to be $1.20 - $1.30.

* Consolidated adjusted Results. See appendix for reconciliation to comparable GAAP results.

CORPORATE PARTICIPANTS

John Stroup Belden, Inc. - President, CEO
Henk Derksen Belden, Inc. - CFO, SVP-Finance
Matt Tractenberg Belden, Inc. – VP, Investor Relations

PRESENTATION

Matt Tractenberg Belden, Inc. – VP, Investor Relations

Thank you, operator. Good morning, everyone, and thank you for joining us today for Belden's first quarter, 2016 earnings conference call.

My name is Matt Tractenberg, I'm Belden's Vice President of Investor Relations. With me this morning are John Stroup, President and CEO, and Henk Derksen, Belden's CFO. John will provide a strategic overview of our business, and then Henk will provide a detailed review of our financial and operating results, followed by Q&A.

We issued our earnings release earlier this morning, and we've prepared a slide presentation that we'll reference on this call. The press release, presentation, and transcript of these prepared remarks are currently available online at investor.belden.com.

Turning to slide 2 in the presentation.

During this call management will make certain forward looking statements. I'd like to remind you that any forward looking information we provide is given in reliance upon the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995. The comments we will make today are management's best judgment based on information currently available. Actual results could differ materially from any forward looking statements that we make, and the Company disclaims any obligation to update this information to reflect future developments after this call. For a more complete discussion of factors that could have an impact on the company's actual results, please review today's press release and our annual report on Form 10-K.

Additionally, during today's call management will reference adjusted or non-GAAP financial information. In accordance with Regulation G, we have provided a reconciliation of the most closely associated GAAP financial information to the non-GAAP financial information we communicate. This reconciliation is in the appendix of the presentation and has been posted separately to the investor relations section of our Web site.

I will now turn the call over to our President and CEO, John Stroup. John?

John Stroup Belden, Inc. – President, CEO

Thank you, Matt, and good morning, everyone.

As a reminder, I'll be referring to adjusted results today.

Please turn to Slide 3 in our presentation for a review of our first quarter highlights.

We are extremely pleased with our first quarter results, including earnings growth, margin expansion, and cash flow. This allowed us to pay down an additional $51 million of debt, further reducing our leverage. Debt reduction continues to be a priority this year, and we're on track to deliver approximately 3.0 times net debt to EBITDA in 2016.

As expected, strength within Broadband, Enterprise, and Network Security markets, offset weakness from our industrial platforms. Despite a difficult year-over-year comparison due primarily to lower oil prices and a stronger U.S. dollar, our attractive portfolio, superior business system, and talented team enabled us to outperform.

I'd like to thank our associates for their hard work during the quarter and their commitment to aggressively executing our strategic plan.

Overall, the business is off to a solid start for the year, with revenues in the first quarter totaling $543.8 million. After adjusting for changes in copper and currency, revenues declined organically by 1.0%. We're encouraged by a consolidated book-to-bill above 1, with industrial orders consistent with seasonal patterns. Year-over-year revenues for the combined industrial platforms, declined by 5.8%, in-line with both expectations and peer results. Our broadband connectivity business and Enterprise and Network Security platforms delivered solid growth within the quarter.

Gross profit margins were 42.3% for the first quarter, an increase of 170 basis points from the year-ago period.

I'm also pleased with our EBITDA margins in the first quarter, at 16.4%, a year-over-year increase of 90 basis points. Free-cash flow in the period improved by almost $63 million dollars from the prior year. I believe this is a great indicator of our commitment to operational excellence and commitment to reducing financial leverage.

Earnings per diluted share was $1.01 in the first quarter, which both exceeded our own estimates and grew slightly from the year-ago period.

As a result of this strong start to the year, we have increased our full-year revenue and EPS guidance.

Please turn to slide 4 for a review of our business segment results.

To capitalize on the adoption of IP technology and accelerate our penetration of the commercial audio-video market, we elected to transfer the responsibility of this product category to our Enterprise segment leadership team. As a result, audio-video cable and connector revenue will now be recognized within the Enterprise Connectivity platform. It was previously recorded within the Broadcast Solutions platform. Prior period segment information has been revised to conform to the change in the composition of reportable segments and is included as an appendix to this release.

Broadcast revenue in the quarter was $171.3 million dollars as compared to $176.5 million in the year ago period. On an organic basis, revenues declined by 2.1% year-over-year. Our strategy and offering continues to be well received, and I'm proud to announce that in April, Grass Valley won the largest project in its history. Our IP introduction continues to gain traction with leading broadcasters around the world, as evidenced by the additional 7 IP systems shipped during the quarter. Additionally, our broadband business continues to perform well, as MSOs invest heavily to keep up with the consumer demand for video. EBITDA margins during the quarter were 13.6%, increasing 50 basis points from the prior-year period and in-line with typical seasonal patterns.

Revenue within our Enterprise platform was $135.9 million. On an organic basis, revenues increased by 4.1%, and orders by 8% year over year. EBITDA margins were 17.5% during the quarter, an increase of 340 basis points from the prior year period. The strength and consistency of this Platform is clearly the result of our team crisply executing a well-crafted strategic plan.

While our Industrial platforms experienced the market softness that we anticipated and discussed with you in prior periods, the productivity measures will mitigate much of the impact to earnings. Combined revenues of $195 million declined by 5.8% from the year-ago period. The organic decline was a result of continued softness within Oil and Gas applications, and broad weakness in Latin America.

Industrial Connectivity had revenue for the quarter of $141.1 million, down 4.1% organically from the year-ago period. EBITDA margins were 16.3% for the first quarter, up 50 basis points, and a solid outcome given the demand headwinds it's facing.

Industrial IT had revenue of $53.9 million, a decrease of 10.2% organically from the first quarter of 2015. Oil and gas applications continue to weigh on the platform, declining by 27%. However, I'm encouraged by a solid book-to-bill of approximately 1.06, driven by strong demand from discrete applications within the EMEA region. As a result of lower volume, EBITDA margins decreased 220 basis points from the year-ago period.

The productivity initiatives introduced last quarter for the Industrial platforms are on track to deliver $6 million of saving in 2016, and $17 million in 2017.

And finally, our Network Security platform increased revenues by 12.1% organically to $41.7 million. Non-renewal bookings during the quarter increased by more than 30%. This is obviously extremely encouraging. In addition to posting outstanding results, Tripwire had a very busy quarter, first, announcing the release of Tripwire Connect, a reporting, analytic and visualization tool that customers can use to manage the increasing complexity of cybersecurity threats. Then, at RSA, they announced a partnership with FireEye to provide integrated industrial network security solutions to critical infrastructure providers around the world. This will further enhance our unique position in the Industrial markets to create leading cybersecurity solutions for global automation partners and other critical infrastructure. And finally, they continue to win customers within the fast growing utility market, with year-over-year growth exceeding 50%. EBITDA margins in the quarter were 27.5%. I'm encouraged by these new innovative products, an expanded customer list, and new industry-leading partners that will allow us to meet the critical security needs of the marketplace.

I will now ask Henk to provide additional insight into our first quarter financial performance. Henk?

Henk Derksen Belden, Inc. - CFO, SVP-Finance

Thank you, John. I will start my comments with results for the quarter, followed by a review of our segment results, a discussion of the balance sheet, and close with our cash flow performance. As a reminder, I will be referencing adjusted results today.

Please turn to Slide 5 for a detailed consolidated review.

First quarter revenues were $543.8 million dollars, a decrease of $25.7 million or 4.5% from $569.5 million in the first quarter 2015. Currency translation and copper unfavorably impacted revenues by $10.9 and $10.4 million respectively. The acquisition of a fiber solutions company increased our revenues by $1.5 million dollars. On an organic basis, revenues declined 1.0% from the year-ago period.

Gross profit margins for the quarter were 42.3%, increasing 170 basis points from the year-ago period, a function of improved productivity. Sequentially, gross profit margins declined 80 basis points in line with typical seasonal patterns.

First quarter SG&A expenses were $116.2 million dollars, or 21.4% of revenue. After adjusting for the impacts of currency and acquisitions, SG&A expenses declined by $1.5 million year-over-year and $5.9 million sequentially. On a year-over-year basis, savings from our Broadcast productivity programs of $5.5 million more than offset continued investment in our Network Security and Enterprise initiatives.

R&D expenses for the quarter were $35.9 million dollars, or 6.6% of revenue. After adjusting for the impact of currency, R&D increased $2.0 million year-over-year, reflective of our continued focus on innovative solutions for our customers.

EBITDA margins were 16.4%, up 90 basis points year-over-year. Our Enterprise, Broadcast, Network Security and Industrial connectivity platforms all contributed to this expansion. Despite a decline in revenues from the year-ago period, EBITDA dollars increased slightly to $89.1 million, highlighting the resilience in our business model. Sequentially, EBITDA margins decreased 260 basis points, driven by seasonally lower volume.

Net interest expense was $24.4 million dollars, an increase of $600,000 dollars year-over-year. The lower debt principal, reduced interest expense by approximately $1.0 million in the quarter. This was more than offset by additional days, which had an unfavorable impact of $1.6 million. We expect interest expense of approximately $24.0 million for the second quarter and $95.0 million for the full year.

The adjusted effective tax rate for the first quarter was 20.0% compared to 18.8% in the prior year. For financial modeling purposes, we recommend using a 20% effective tax rate for the second quarter and full year 2016.

Earnings per diluted share was $1.01 compared to $1.00 in the year-ago period.

Please turn to slide 6.

I will now discuss revenues and operating results by business segment.

As a reminder, our audio-video cable and connector results will now be recognized within the Enterprise Connectivity Platform. After adjusting for the change, Broadcast Solutions generated revenues of $171.3 million dollars during the first quarter. Compared to the year-ago period, revenues decreased $5.2 million. Currency translation unfavorably impacted revenues by $3.0 million and the acquired fiber solutions company contributed $1.5 million. On an organic basis, revenues declined 2.1% from the year-ago period. Sequentially, revenues decreased in line with typical seasonal patterns.

Broadcast EBITDA margins improved year-over-year by 50 basis points to 13.6% of revenues. Sequentially, EBITDA margins declined 630 basis points, mainly a result of seasonally lower volume.

Our Enterprise Connectivity segment generated revenues of $135.9 million dollars during the first quarter, a decrease of $5.9 million year-over-year. This segment faced a $2.9 million headwind from currency translation and a $5.0 million unfavorable impact from lower copper prices. Organic growth in the quarter was 4.1% year-over-year with all major regions expanding.

The Enterprise segment generated EBITDA margins of 17.5%, an increase of 340 basis points from the year ago period. This segment benefitted from leverage on volume and improved productivity. Sequentially, EBITDA margins increased 70 basis points due to productivity.

The Industrial Connectivity segment generated revenues of $141.1 million dollars in the quarter. Currency translation and copper prices unfavorably impacted revenues by $4.1 million and $5.3 million respectively from the year-ago period. On an organic basis, revenues declined 4.1% year-over-year and 2.1% sequentially.

EBITDA margins of 16.3% increased 50 basis points year-over-year, primarily due to productivity. Sequentially, EBITDA margins declined 50 basis points as a result of mix.

The Industrial IT segment generated revenues of $53.9 million dollars. Currency translation unfavorably impacted the segment by $1.0 million year-over-year. On an organic basis, revenues declined 10.2% from the prior-year period and 14.4% sequentially. While the sequential decline is a function of typical seasonality, the year over-year decline is primarily due to softer Oil & Gas Markets. As John mentioned, we are encouraged by our book-to-bill ratio of 1.06 for the quarter.

EBITDA margins of 16.0% declined 220 basis points year-over-year and 240 basis points sequentially. This was mainly a function of leverage on lower volume. As we execute on our productivity improvement programs, we expect EBITDA margins for this platform to be at approximately 18.0% on a full-year basis.

Finally, our Network Security segment continues to perform well, generating revenues of $41.7 million dollars, up 12.1% on an organic basis year-over-year. Sequentially, revenues declined 15.0%, reflecting the seasonality of this business.

EBITDA margins were 27.5%, an improvement of 80 basis points from the year ago period, a result of leverage on volume partially offset by strategic investments.

If you will please turn to Slide 7, I will begin with our balance sheet highlights.

Our cash and cash equivalents balance at the end of the first quarter was $146 million dollars compared to $217 million in the prior quarter, and $167 million in the prior year. During the first quarter we paid down $51 million of our outstanding debt, reducing our total debt principal amount to $1.72 billion.

Inventory turnover was 5.9 turns, down 1.2 turns sequentially, and up 0.2 turns on a year-over-year basis.

Days sales outstanding was 60 days in the first quarter, an improvement of 2 days sequentially and 3 days year-over-year.

PP&E turnover was 6.8 turns, down 0.9 turns sequentially and 0.1 turns year-over-year.

Net leverage was 3.7 times net debt to EBITDA at the end of the quarter. We are on track to achieve a net leverage ratio of approximately 3.0 times by the end of 2016.

Please turn to Slide 8 for a few cash flow highlights.

Cash flows from operations were $12.7 million dollars, an increase of $60.9 million dollars from the prior-year period. This was mainly driven by improvements in our operating working capital performance, with an impact of approximately $54 million.

Net capital expenditure for the quarter was $13.4 million, decreasing $2.1 million year-over-year.

Free cash flow was a use of $700,000 and improved by $63 million from the year-ago period.
That completes my prepared remarks. I would now like to turn this call back to our CEO, John Stroup, for the outlook. John?

John Stroup Belden, Inc. – President, CEO

Thank you, Henk.

Please turn to Slide 9 for our outlook regarding the second quarter and full-year 2016 results.

Given the strong start, we have increased our revenue and earnings outlook for the year. We expect our Broadband, Enterprise, and Network Security businesses will continue to perform well and benefit from favorable end-market conditions. Although our industrial businesses are down year-over-year, sequential performance, backlog, and order rates suggest stability that should lead to a better second half.

We anticipate second quarter 2016 revenues to be between $570 and $590 million, and EPS is expected to be between $1.20 and $1.30.

For the full year, we now expect revenues between $2.320 and $2.370 billion. The expected range of EPS is now $5.15 to $5.45.

That concludes our prepared remarks, operator please open the call to questions.