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1st Quarter 2019 Earnings Transcript

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CORPORATE PARTICIPANTS

John Stroup Belden, Inc. – President, CEO, and Chairman
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PRESENTATION

Kevin Maczka Belden, Inc. – VP, Treasurer & Investor Relations

Thank you, operator. Good morning, everyone, and thank you for joining us today for Belden's first quarter 2019 earnings conference call.

My name is Kevin Maczka, I'm Belden's Vice President, Treasurer and Investor Relations. With me this morning are John Stroup, President, CEO, and Chairman, 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 have prepared a slide presentation that we will 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 in reliance upon the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995. For more information, 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, the appendix to our presentation and the investor relations section of our website contain a reconciliation of the most closely associated GAAP financial information to the non-GAAP financial information we communicate.

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

John Stroup Belden, Inc. – President, CEO, and Chairman

Thank you, Kevin, 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 performance.

Revenues were consistent with our expectations in the quarter, and we delivered EPS near the high end of our guidance range.

First quarter revenues declined 1.7% on organic basis to $587.2 million. As a reminder, results in the first quarter 2018 benefitted from non-recurring revenue recognition timing. After adjusting for that impact, revenues increased 2.8% organically.

EBITDA was $87.1 million, reflecting 14.8% EBITDA margins.

EPS was $0.99, compared to the guidance range of $0.80 to $1.00.

I am pleased to report significantly improved free cash flow. Free cash flow increased $30 million year-over-year in the first quarter.

Further, free cash flow increased $108 million on a trailing twelve month basis, from $115 million in the first quarter 2018 to $223 million in the first quarter 2019.

We also completed two strategic acquisitions subsequent to the end of the first quarter. We acquired Opterna and the FutureLink product line of Suttle, Inc. for a combined purchase price of approximately $50 million. These two broadband fiber businesses complement our product roadmap with a set of innovative fiber connectivity solutions that should enable further growth and share capture in our PPC broadband business.

Overall, we are on track to meet our commitments for 2019, and we are raising the low end of our full-year guidance ranges.

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

I will begin with our Enterprise Solutions segment. As a reminder, our Enterprise solutions allow customers to transmit and secure data, sound, and video across complex enterprise and media networks. Our key markets include smart buildings, final mile broadband, and live media production.

After adjusting for the non-recurring revenue recognition timing in the year-ago period, revenues in this segment increased 30 basis points on an organic basis to $326.5 million.

Revenues in the smart building market increased 5% organically. This robust growth was a function of improved pricing and continued share capture.

This market continues to benefit from healthy non-residential construction in the United States, and increased needs for contractor productivity and building efficiency.

This trend is best reflected by our innovative Category 6A cable products, which deliver both data and power over Ethernet. Category 6A systems revenue increased 15% organically in the first quarter.

Revenues in final mile broadband declined 6% year-over-year in the first quarter.

We continue to see robust growth with our fiber optic and our outside-the-home products, which benefit from increasing broadband subscribers and network upgrades, but demand for products used inside-the-home remains softer.

Importantly, following the two recent acquisitions, the majority of our broadband revenues come from outside-the-home products. We continue to pursue additional organic and inorganic opportunities that would allow us to further expand our fiber product offering and drive substantial growth.

Revenues in live media production were approximately flat when adjusted for the revenue recognition timing in the first quarter of 2018.

Enterprise Solutions segment EBITDA margins were 12.1%.

Turning now to our Industrial segment. Much like Enterprise, our Industrial solutions allow customers to transmit and secure data, sound, and video, but in this case in harsh industrial environments. Our key markets include discrete manufacturing, process facilities, energy, and transportation.

Revenues in this segment increased 6.0% on an organic basis to $260.7 million.

Demand was broad-based with growth in all regions, and particular strength in our process end markets during the quarter. We continue to benefit from a balanced portfolio of industrial businesses.

Cybersecurity demand trends remain very encouraging, with a notable acceleration in revenue and bookings growth during the quarter. Revenues increased 11% organically on a year-over-year basis and non-renewal bookings, our best leading indicator of revenues, increased a very strong 40%. This represents the third consecutive quarter of robust growth in non-renewal bookings, which increased 17% in the second half of 2018.

Our new Cloud-based solutions continue to gain traction with new and existing customers. During the quarter, we secured our largest cybersecurity order ever with a Cloud-based product for a new customer.

We anticipate further solid growth in this business going forward as we continue to develop and launch new products to expand our comprehensive suite of solutions specifically designed for industrial and enterprise applications.

Industrial Solutions segment EBITDA margins of 18.2% were consistent with the year ago period.

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….

Revenues were $587.2 million dollars in the quarter, decreasing $20.2 million, or 3.3%, from $607.4 million in the first quarter of 2018.

Revenues were favorably impacted by $8.9 million from acquisitions, and negatively impacted by $18.8 million from currency translation and lower copper prices. After adjusting for these factors, revenues decreased 1.7% organically from the prior-year period.

Please note that the prior-year period was favorably impacted by $27 million dollars related to previously disclosed, non-recurring revenue recognition timing. After adjusting for this impact, revenues increased 2.8% organically on a year-over-year basis.

Gross profit margins in the quarter were 38.5%, decreasing 140 basis points compared to 39.9% in the year-ago period.

Operating expenses were $152.4 million dollars, or 26.0% of revenues.

EBITDA was $87.1 million dollars, decreasing $16.2 million, or 15.7%, compared to $103.3 million in the prior-year period.

EBITDA margins were 14.8%, decreasing 220 basis points year-over-year. The first quarter 2018 included a non-recurring benefit of approximately 200 basis points related to revenue recognition timing. After adjusting for this impact, EBITDA margins were consistent with the prior year.

Net interest expense declined $2.8 million dollars year-over-year to $14.2 million, as a result of the successful debt refinancing actions completed in early 2018.

As a reminder, our debt is entirely fixed at an average interest rate of 3.5% with no maturities until 2025 to 2028.

At current foreign exchange rates, we expect interest expense of $58 million dollars for the full year 2019, down from $62 million in 2018.

Our effective tax rate was 20.0% in the quarter, compared to 22.8% in the first quarter 2018.

For financial modeling purposes, we recommend using an effective tax rate of 18% for the second quarter and 20% for the full year 2019.

Net income was $48.1 million dollars, compared to $57.5 million in the prior-year period.

Earnings per share was $0.99 in the quarter, compared to $1.16 in the year-ago period.

As a reminder, prior-year EPS included a $0.29 non-recurring benefit related to revenue recognition timing.

Please turn to slide 6. I will now discuss revenues and operating results by business segment.

Our Enterprise Solutions segment generated revenues of $326.5 million dollars during the quarter, decreasing 7.0% from the prior-year period.

Revenues were favorably impacted by $8.9 million dollars from acquisitions, and negatively impacted by $7.6 million from currency translation and copper prices. After adjusting for these factors, revenues decreased 7.3% organically on a year-over-year basis.

Excluding the revenue recognition impact in the prior-year period that I mentioned previously, revenues increased 30 basis points organically.

EBITDA margins were 12.1% in the quarter, declining 430 basis points from the prior year period. This decline resulted primarily from the revenue recognition timing in the year-ago period.

The Industrial Solutions segment generated revenues of $260.7 million dollars in the quarter, increasing 1.7% from the prior-year period. Currency translation and copper prices had a negative impact of $11.2 million dollars. After adjusting for these factors, revenues increased 6.0% organically.

We continued to see broad-based demand in our industrial markets during the quarter, with revenue growth in all regions.

EBITDA margins were 18.2% in the quarter, consistent with the prior year.

We continue to make strategic investments in new products which are expected to drive growth in future periods. We are already seeing positive results from some of these important investments, such as our new Cloud-based cybersecurity solutions. We are very encouraged by the accelerating momentum in our cybersecurity non-renewal bookings, which increased 17% in the second half of 2018 and a very robust 40% in the first quarter of 2019.

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 $339 million dollars compared to $421 million in the fourth quarter and $363 million in the prior year period.

Working capital turns were 5.8 turns, compared to 9.5 turns in the prior quarter and 5.7 turns in the prior-year.

Days sales outstanding improved 4 days on a year-over-year basis, from 66 days in the prior year period to 62 days.

Inventory turns were 4.4 turns, compared to 4.6 turns in the first quarter of 2018.

Our total debt principal at the end of the first quarter was $1.46 billion, compared to $1.49 billion in the fourth quarter and $1.69 billion in the year-ago period.

Net leverage was 2.4 times net debt to EBITDA at the end of the quarter, down from 2.9 times in the first quarter of 2018 and in-line with our target range of 2.0 – 3.0 times.

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

Cash flow from operations in the first quarter was a use of $46.1 million dollars, improving $37.8 million dollars compared to a use of $83.9 million in the prior year.

Net capital expenditures were $23.6 million for the quarter, compared to $15.9 million from the prior-year period. During the quarter, we invested in capacity expansions in our industrial and broadband fiber businesses to reduce lead times and support customer demand.

Free cash flow in the quarter was a use of $69.6 million dollars, improving $30.1 million dollars compared to a use of $99.7 million in the prior-year period.

Further, free cash flow increased $108 million on a trailing twelve month basis, from $115 million in the first quarter 2018 to $223 million in the first quarter 2019. We are very pleased with these significant gains, which resulted from improvements in our EBITDA, working capital, and capital structure.

For the full-year 2019, we expect free cash flow in the range of $220 to $240 million dollars. This outlook represents an increase of 14-24% compared to $193 million in 2018.

Finally, we completed two strategic acquisitions in our PPC broadband business subsequent to the end of the first quarter. We acquired Opterna and the FutureLink product line of Suttle, Inc. for a combined purchase price of approximately $50 million.

We expect these acquisitions to achieve our typical ROIC targets and contribute approximately $25 million in revenue in 2019.

That completes my prepared remarks. I would now like to turn this call back to our President, CEO, and Chairman, John Stroup, for the outlook. John?

John Stroup's Guidance Remarks

Thank you, Henk.

Please turn to Slide 9 for our outlook.

We are on track to meet our commitments for 2019, and we are raising the low end of our full-year guidance ranges.

We anticipate second quarter 2019 revenues to be between $630 and $660 million, and EPS of $1.30 to $1.50.

For the full year 2019, we now expect revenues to be between $2.520 billion and $2.595 billion, compared to our prior guidance range of between $2.495 billion and $2.595 billion. We now expect full year EPS of $5.65 to $6.15, compared to our prior guidance range of $5.50 to $6.15.

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