CTS Corporation 3rd Quarter 2022 Earnings Call

Oct 26, 2022









Forward-Looking Statements

This document contains statements that are, or may be deemed to be, forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements include, but are not limited to, any financial or other guidance, statements that reflect our current expectations concerning future results and events, and any other statements that are not based solely on historical fact. Forward-looking statements are based on management's expectations, certain assumptions and currently available information. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof and are based on various assumptions as to future events, the occurrence of which necessarily are subject to uncertainties. These forward-looking statements are made subject to certain risks, uncertainties and other factors, which could cause CTS' actual results, performance or achievements to differ materially from those presented in the forward-looking statements. Examples of factors that may affect future operating results and financial condition include, but are not limited to: the ultimate impact of the COVID-19 pandemic on CTS' business, results of operations or financial condition, including supply chain disruption; changes in the economy generally**,** including inflationary and/or recessionary conditions, and in respect to the business in which CTS operates; unanticipated issues in integrating acquisitions**,** including TEWA Temperature Sensors and Ferroperm Piezoceramics; the results of actions to reposition CTS' business; rapid technological change; general market conditions in the transportation, as well as conditions in the industrial, aerospace and defense, and medical markets; reliance on key customers; unanticipated public health crises, natural disasters or other events; environmental compliance and remediation expenses; the ability to protect CTS' intellectual property; pricing pressures and demand for CTS' products; and risks associated with CTS' international operations, including trade and tariff barriers, exchange rates and political and geopolitical risks (including, without limitation, the potential impact U.S./China relations and the conflict between Russia and Ukraine may have on our business, results of operations and financial condition). Many of these, and other risks and uncertainties, are discussed in further detail in Item 1A. of CTS' most recent Annual Report on Form 10-K and other filings made with the SEC. CTS undertakes no obligation to publicly update CTS' forward-looking statements to reflect new information or events or circumstances that arise after the date hereof, including market or industry changes.

Non-GAAP Financial Measures

From time to time, CTS may use non-GAAP financial measures in discussing CTS' business. These measures are intended to supplement, not replace, CTS' presentation of its financial results in accordance with U.S. GAAP. CTS' management believes that non-GAAP financial measures can be useful to investors in analyzing CTS' financial performance and results of operations over time. CTS recommends that investors consider both actual and adjusted measures in evaluating the performance of CTS with peer companies. The information included in this presentation includes the non-GAAP financial measures of adjusted gross margin, adjusted operating earnings, adjusted EBITDA margin, adjusted net earnings, adjusted diluted earnings per share, debt to capitalization ratio, controllable working capital ratio, and free cash flow. Many of these non-GAAP financial measures exclude the effect of certain expenses and income not related directly to the underlying performance of CTS' fundamental business operations. CTS believes that adjusted gross margin, adjusted operating earnings, adjusted EBITDA margin, adjusted net earnings and, adjusted diluted earnings per share provide useful information to investors regarding its operational performance because they enhance an investor's overall understanding of CTS' core financial performance and facilitate comparisons to historical results of operations, by excluding items that are not related directly to the underlying performance of CTS' fundamental business operations or were not part of CTS' business operations during a comparable period. CTS believes that debt to capitalization ratio is a measurement of financial leverage and provides an insight into the financial structure of CTS and its financial strength. CTS believes the controllable working capital ratio provides an objective measure of the efficiency with which CTS manages its short-term capital needs. CTS believes that free cash flow is a useful measure of its ability to generate cash. CTS believes that these non-GAAP financial measures are commonly used by financial analysts and others in the industries in which CTS operates, and thus further provide useful information to investors. Note that CTS' definitions of these non-GAAP financial measures may differ from those terms as defined or used by other companies. CTS does not provide reconciliations of forward-looking non-GAAP financial measures, such as estimated adjusted diluted earnings per share, to the most comparable GAAP financial measures on a forward-looking basis because CTS is unable to provide a meaningful or accurate calculation or estimation of reconciling items and the information is not available without unreasonable effort. This is due to the inherent difficulty of forecasting the timing and amount of certain items, such as, but not limited to, restructuring costs, environmental remediation costs, acquisition related costs, foreign exchange rates and other non-routine costs. Each of such adjustments has not yet occurred, are out of CTS' control and/or cannot be reasonably predicted. For the same reasons, CTS is unable to address the probable significance of the unavailable information.

Q3 2022 – Executing diversification strategy to deliver revenue and earnings growth

Third Quarter		
$152M	36.6%	$0.62
Sales	Adj. Gross Margin	Adj. diluted EPS
+24.1%	(70) bps	+33.8%

All comparisons vs. same period in prior year unless otherwise noted

- Organic growth +17.1%
- Non-transportation revenues +22.5%, organic 8.2%
- Acquisitions added $8.6m in sales in 3Q
- Transportation revenues +25.7%
- New business wins $159M, 6 EV platform wins
- Adj. EBITDA Margin 22.3%, up 60 bps from Q3 2021

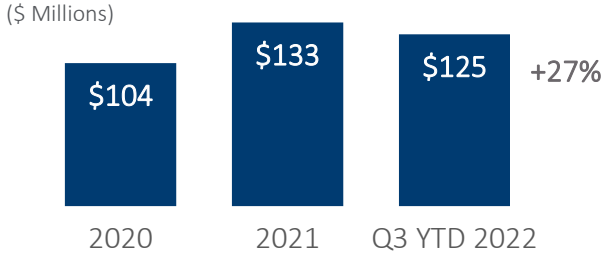
Operational discipline supporting strong financial performance

Establishing leadership in non-transportation end markets

Industrial

Revenue

($ Millions)







Added new customers in nano-positioning and EMC application in rail transportation

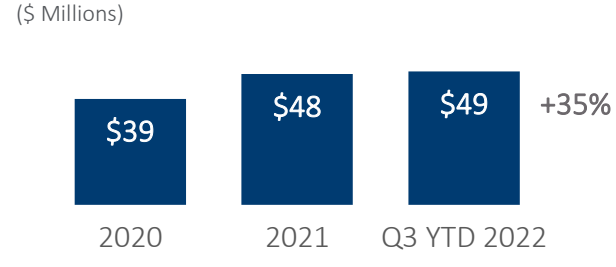
Ongoing momentum for HVAC, industrial appliances



Medical

Revenue

($ Millions)









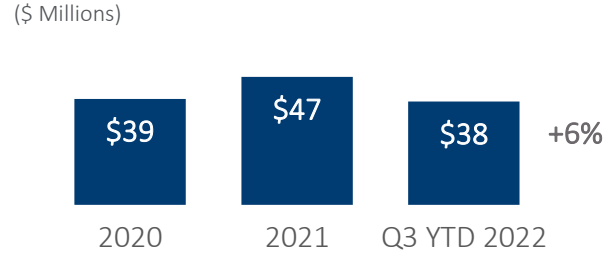
Commercial focus driving expanded customer base

New awards in drug delivery for liver ablation and minimally invasive surgery

Aerospace & Defense

Revenue

($ Millions)









Gaining traction in European defense market through support of Ferroperm team

New awards in unmanned underwater vehicle application, low orbit satellite application

Capturing secular trends to expand into premium, growing markets

Strategic acquisitions fueling diversification – M&A as a catalyst

Enhancing Piezoceramic Technology and Geographic Reach

Pre 2016	2016	2017	2022	Current
CTS	HC Materials Channel Technologies Advanced Materials Division	noliac	Ferroperm Piezoceramics	CTS
Bulk Technology	Single Crystal Technology	Tape Cast Technology	Medical Therapeutics Europe Defense	Growing Piezoceramic Platform

Building a Strong Global Temperature Sensing Platform

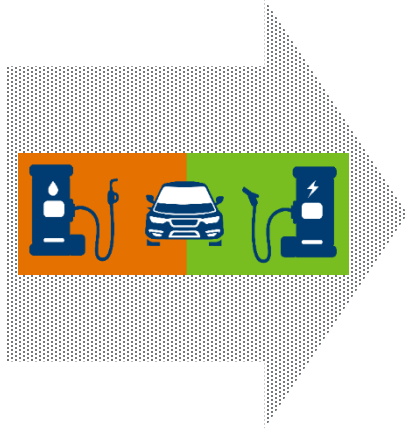
2019	2020	2022	Current
QTI Sensing Solutions	Sensor Scientific, Inc.	TEWA Temperature Sensors	CTS
Industrial Applications	Medical Applications	Industrial + Medical Europe Expansion	Growing Temperature Platform

Ferroperm complements existing CTS piezoceramic capabilities

>95% Light Vehicle portfolio carries over to Electric Vehicles

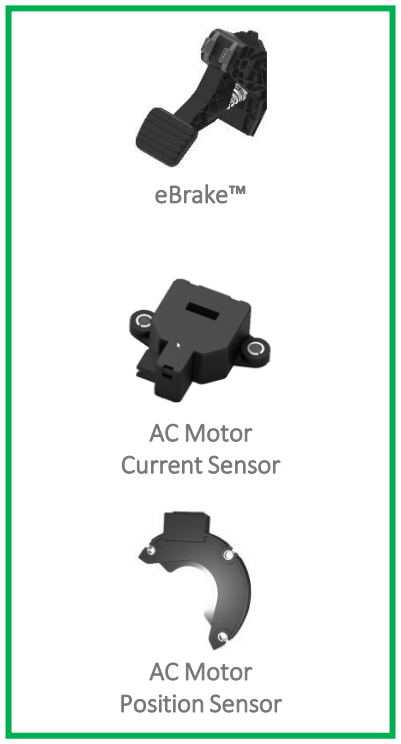
CTS Portfolio







+



Available Market (SAM)

2022:
$2.4Bn
Traditional light vehicle key product Portfolio

2030:
$2.7Bn
Light vehicle key products For BEV/HEV/PHEV and ICE

+

>2030:
$1Bn+
New products for Electrification

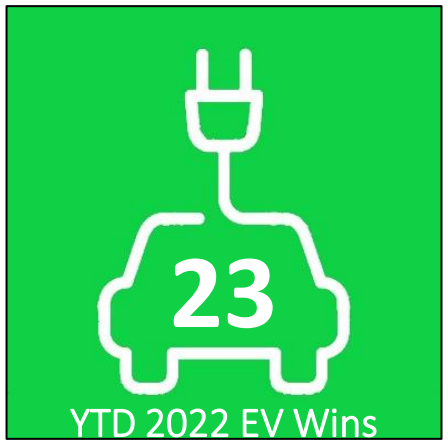
>$1Bn expansion in Available Market with EV-related new products

6 Battery Electric Vehicle Platform wins in Q3 2022 – Total 23 in 2022, 44 Total















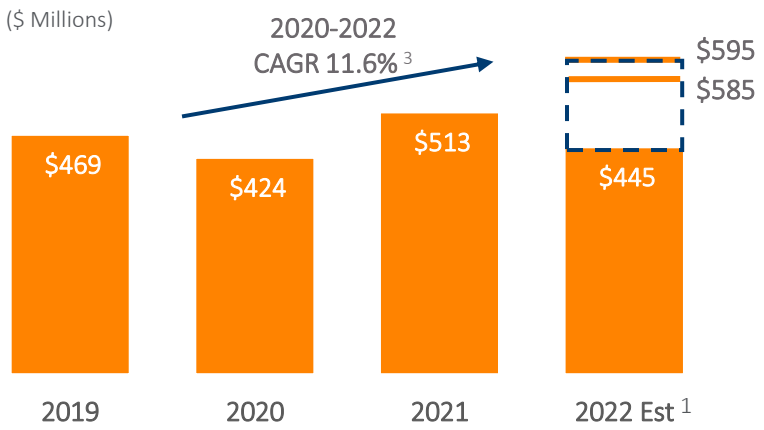
~8% of 2022 light vehicle sales from BEV+Hybrid platforms, Goal: >25% by 2025

FY 2022 Guidance

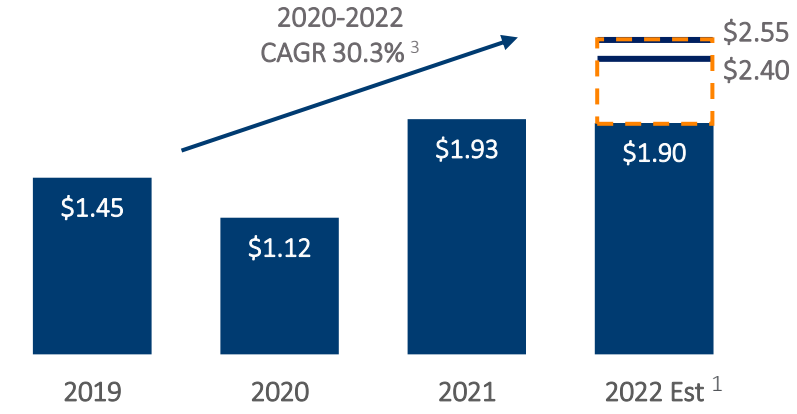
Key Outlook Assumptions

- Strong demand from medical & aerospace/defense customers
- Softer outlook in industrial end market & distribution channel
- Commercial vehicle sales potentially impacted by semiconductor supply issues
- Light vehicle market forecasts - US 13.5 -14M, China 24.5-25M, Europe 15-16M units, lowered from earlier this year
- Monitoring risks from interest rates, supply challenges, inflation, COVID-19, FX fluctuations & geopolitical landscape
- Tax rate in the range of 20-23% excluding discrete items

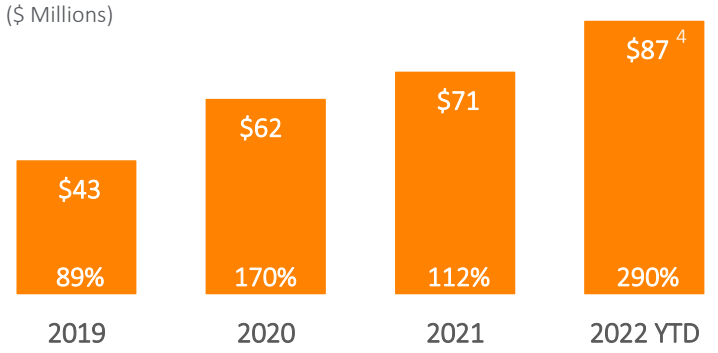
Revenue



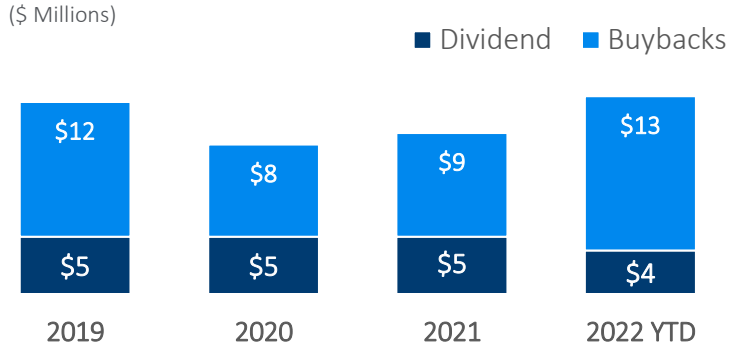
Adj. Diluted EPS



Free Cash Flow Conversion[2]



Returned to Shareholders



Note:

[1] Guidance includes recent Ferroperm acquisition
[2] Free cashflow conversion = FCF / Adjusted Net Earnings
[3] CAGR based on mid point of 2022 guidance
[4] Includes $34M from U.S. pension plan termination

Your Partner in Smart Solutions

3rd Quarter 2022 Financial Results

Q3 2022 Financial Summary

Revenue
($ millions)



	Q3 2021	Q2 2022	Q3 2022
Net Income ($'Mil)	$(63.9)	$12.6	$11.8
Diluted EPS	$(1.97)	$0.39	$0.37
Adj. Diluted EPS	$0.46	$0.62	$0.62
Adj. Gross Margin	37.3%	36.1%	36.6%
Adj. EBITDA Margin	21.7%	21.4%	22.3%

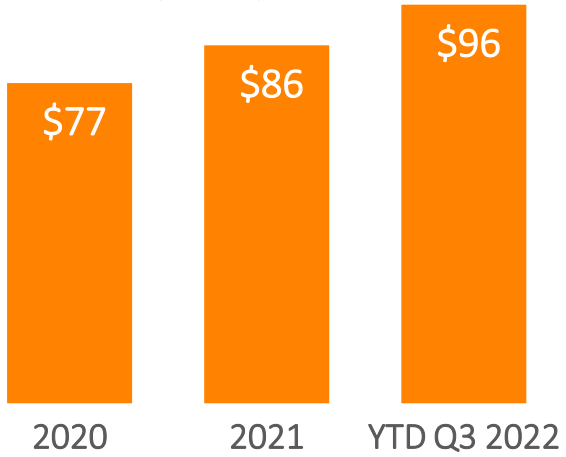
Highlights

- Revenue up 24.1% vs. Q3 2021, up 4.8% vs. Q2 2022
- Non-transportation sales up 22.5% vs. Q3 2021, organic growth +8.2%
- Transportation sales up 25.7% vs. Q3 2021, up 4.9% vs. Q2 2022
- Currency impact on sales unfavorable $4.1m
- Adjusted EBITDA margin +60 bps to 22.3%
- Continued margin pressure from supply challenges, currency, cost increases; partially mitigated by pricing and continuous improvement projects

Consistent strong cash flow generation

Operating Cash Flow

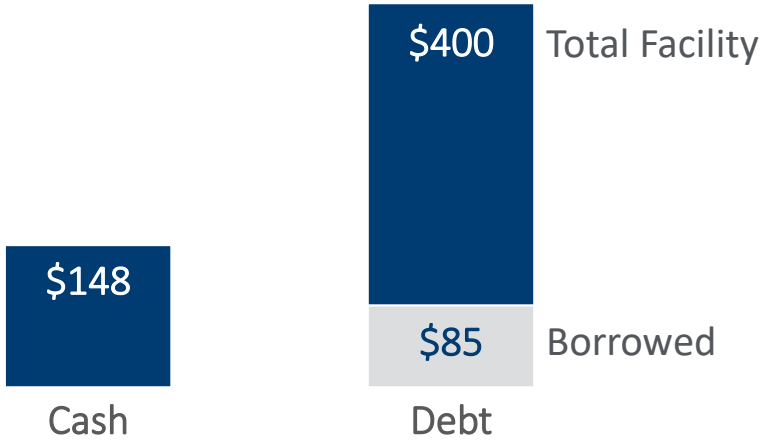
($ Millions)



Note: YTD 2022 results include $34m from US pension plan termination

Cash and Debt

($ Millions)



Note: Cash and Debt balance as of Sep 30, 2022

Q3 2022 – $58M
YTD 2022 – $86M
Free Cash Flow

Q3 2022 – $3M
YTD 2022 – $17M
Returned to shareholders

Q3 2022 – $2M
YTD 2022 – $9M
Capital Expenditures

Strong Balance Sheet
Solid Foundation for Strategic M&A

Q & A

Appendix

Regulation G Schedules

Adjusted Diluted EPS

	Q3		Q2	Q1	Year-to-Date		Full Year		
	2022	2021	2022	2022	2022	2021	2021	2020	2019
Diluted earnings (loss) per share	**$ 0.37**	**$ (1.97)**	**$ 0.39**	**$ 0.63**	**$ 1.38**	**$ (1.58)**	**$(1.30)**	**$1.06**	**$1.09**
Tax affected adjustments to reported diluted earnings (loss) per share:									
Restructuring charges	0.01	0.01	0.02	0.01	0.04	0.02	0.06	0.04	0.18
Foreign currency loss (gain)	0.01	0.03	0.12	(0.01)	0.12	0.04	0.10	(0.16)	0.05
Non-cash pension expense	0.16	2.54	-	-	0.16	3.10	3.13	0.06	0.02
Environmental charges	0.01	0.01	0.02	0.01	0.04	0.02	0.05	0.07	0.05
Acquisition-related costs	-	-	0.05	0.02	0.07	-	-	0.01	0.02
Inventory fair value step-up	0.06	-	0.02	0.01	0.09	-	-	-	-
Legal settlement	-	-	-	-	-	-	-	-	(0.01)
Discrete tax items	-	(0.16)	-	-	-	(0.16)	(0.11)	0.04	0.05
Adjusted diluted earnings per share	**$ 0.62**	**$ 0.46**	**$ 0.62**	**$ 0.67**	**$ 1.90**	**$ 1.44**	**$ 1.93**	**$1.12**	**$1.45**

Regulation G Schedules

Adjusted EBITDA

($ Millions, except percentages)

	Q3		Q2	Q1	Year-to-Date		Full Year		
	2022	2021	2022	2022	2022	2021	2021	2020	2019
Net earnings (loss)	$ 11.8	$ (63.9)	$ 12.6	$ 20.2	$ 44.6	$ (51.0)	$ (41.9)	$ 34.7	$ 36.1
Depreciation and amortization expense	8.0	6.7	7.0	6.7	21.7	20.2	26.9	26.7	24.6
Interest expense	0.3	0.5	0.6	0.5	1.5	1.6	2.1	3.3	2.6
Tax expense (benefit)	5.5	(25.9)	4.3	5.5	15.3	(24.6)	(19.0)	10.8	14.1
EBITDA	**25.6**	**(82.6)**	**24.5**	**33.0**	**83.2**	**(53.8)**	**(31.8)**	**75.4**	**77.5**
Adjustments to EBITDA:									
Restructuring charges	0.5	0.3	0.6	0.3	1.4	0.6	1.7	1.8	6.9
Environmental charges	0.3	0.4	0.9	0.5	1.8	0.9	2.3	2.8	2.3
Legal settlement	-	-	-	-	-	-	-	-	(0.5)
Acquisition-related costs	-	-	2.0	0.5	2.5	-	-	0.3	0.7
Inventory fair value step up	2.2	-	0.5	0.6	3.3	-	-	-	-
Costs of tax improvement initiatives	-	-	-	-	-	-	-	-	0.1
Non-cash pension expense	4.7	107.4	-	0.1	4.8	131.1	132.4	2.5	0.8
Foreign currency loss (gain)	0.5	1.0	3.8	(0.3)	4.0	1.4	3.3	(5.3)	1.8
Total adjustments to EBITDA	8.2	109.2	7.9	1.8	17.8	134.0	139.7	2.1	12.0
Adjusted EBITDA	**$ 33.8**	**$ 26.6**	**$ 32.5**	**$ 34.8**	**$ 101.0**	**$ 80.2**	**$ 107.8**	**$ 77.5**	**$ 89.5**
Net sales	$ 151.9	$ 122.4	$ 151.9	$ 147.7	$ 444.6	$ 380.4	$ 512.9	$ 424.1	$ 469.0
Adjusted EBITDA margin	22.3%	21.7%	21.4%	23.6%	22.7%	21.1%	21.0%	18.3%	19.1%

Regulation G Schedules

Adjusted Gross Margin

($ Millions)

	Q3 2022	Q3 2021	Q2 2022
Gross margin	**$ 53.3**	**$ 45.7**	**$ 51.8**
Adjustment to reported gross margin:			
Inventory fair value step-up	$2.2	-	$0.5
Adjusted gross margin	**$ 55.6**	**$ 45.7**	**$ 52.4**
Net sales	$ 151.9	$ 122.4	$ 145.0
Adjusted gross margin as a % of net sales	36.6%	37.3%	36.1%

Regulation G Schedules

Free Cash Flow

($ Millions)

	Q3 2022	Year-to-Date 2022	Full Year 2021	Full Year 2020	Full Year 2019
Net cash provided by operating activities	**$ 60.4**	**$ 95.7**	**$ 86.1**	**$ 76.8**	**$ 64.4**
Capital expenditures	(2.3)	(9.3)	(15.6)	(14.9)	(21.7)
Free cash flow	**$ 58.1**	**$ 86.5**	**$ 70.5**	**$ 61.9**	**$ 42.7**
Free Cash Flow as % of Adjusted Net Earnings	294%	141%	112%	170%	89%

Regulation G Schedules

Debt to Capitalization

($ Millions)

	Q3		As of December 31		
	2022	2021	2021	2020	2019
Total debt **(A)**	$ 85.5	$ 50.0	$ 50.0	$ 54.6	$ 99.7
Total shareholders' equity **(B)**	$ 490.6	$ 457.4	$ 463.6	$ 423.7	$ 405.2
Total capitalization **(A+B)**	$ 576.1	$ 507.4	$ 513.6	$ 478.3	$ 504.9
Total debt to capitalization	**14.8%**	**9.9%**	**9.7%**	**11.4%**	**19.7%**