Operator: Welcome to the Allied Motion Technologies Inc. Second Quarter Fiscal Year 2022 Financial Results Conference Call. I would now like to turn the conference over to Craig Mychajluk, Investor Relations.

Craig Mychajluk: Thank you, and good morning, everyone. We certainly appreciate your time today as well as your interest in Allied Motion. Joining me on the call are Dick Warzala, our Chairman, President and CEO; and Mike Leach, our Chief Financial Officer. Dick and Mike are going to review our second quarter 2022 results and provide an update on the company's strategic progress and outlook, after which we'll open it up for Q&A.

You should have a copy of the financial results that were released yesterday after the market closed. If not, you can find it on our website at alliedmotion.com, along with the slides that accompany today's discussion.

If you are reviewing those slides, please turn to Slide 2 for the safe harbor statement. As you are aware, we may make some forward-looking statements on this call during the formal discussion as well as during the Q&A. These statements apply to future events that are subject to risks and uncertainties as well as other factors that could cause actual results to differ materially from what is stated on today's call. These risks and uncertainties and other factors are discussed in the earnings release as well as with other documents filed by the company with the Securities and Exchange Commission. You can find these documents on our website or at sec.gov.

I want to point out as well that during today's call we'll discuss some non-GAAP measures, which we believe will be useful in evaluating our performance. You should not consider the presentation of this additional information in isolation or as a substitute for results prepared in accordance with GAAP. We have provided reconciliations of non-GAAP to comparable GAAP measures in the tables accompanying the earnings release and slides.

With that, please turn to Slide 3, and I'll turn it over to Dick to begin. Dick?

Dick Warzala: Thank you, Craig, and welcome, everyone. Our results continue to demonstrate the successful execution of our strategic growth initiatives. Second quarter revenue grew 21% to a record $122.7 million with solid organic growth of 10%. Our industrial markets saw strong demand, resulting in market growth of 40% over last year. We are benefiting from new solution offerings, acquisitions and continued economic recovery in broader end market verticals, including industrial automation, oil and gas, material handling, HVAC and instrumentation.

Recent acquisitions also contributed to the Aerospace & Defense market, which doubled from the year ago period. While we are doing well on the top line, the highlight of the quarter was the improvement in our gross margin performance, which is consistent with our stated objectives as we achieved a record level of 32.4%. This was up 170 basis points from a year ago and a significant 320 basis points over the sequential first quarter.

Our M&A activity is certainly helping, but we also equate this performance to our global teams that continue to manage multiple headwinds as supply chain issues and inflationary pressures on logistics, energy, material and labor continue to persist.

Even at the operating level, our performance was solid as we continue to invest for future growth and considering the costs associated with the acquisitions that have not yet been fully leveraged. We achieved adjusted net income per share of $0.36, up 9% from $0.33 per share in the prior-year period.

Our pipeline of opportunities remains high and order levels continue to be strong with a book-to-bill of 1.1x in the second quarter, yielding a record backlog of nearly $324 million. I will talk more to orders and backlog later in the presentation.

We had a busy quarter on the M&A front as we continue to augment our growth and profitability strategy. If you turn to Slide 4, we highlight the three acquisitions we completed in the quarter.

Located in Camarillo, California, ThinGap expands our precision motor capabilities by providing industry-leading high-performance, zero cogging, slotless motors for use in applications in aerospace, defense and medical that require precise motion and a compact high-torque-to-volume package. We also see the potential to advance our total solution capability into robotics, semiconductor and instrumentation markets.

Second, we acquired FPH Group with locations in Ontario, Canada and Michigan. FPH brings technically advanced, reliable and cost-effective electrical drive systems and light weighting technologies for existing and future ground-based vehicles in the defense industry. FPH has a proven relationship with leading defense prime contractors and adds critical manufacturing licenses and certifications, which we believe we can leverage to drive deeper penetration within defense applications.

Lastly, we acquired Airex out of Somersworth, New Hampshire. A company with over 70 years of history, providing high-precision electromagnetic solutions, including linear and rotary motor technology for aerospace and defense, life sciences, semiconductor and other industrial applications. Their patented winding technologies, combined with robotic manufacturing assures best-in-class linear motors as they provide the highest linear force density in the industry and have been selected and utilized in our own Alio solution offerings for many years.

We would like to welcome all the new employees to the Allied family.

In reviewing the six acquisitions since last year's fourth quarter, they add significant new engineering resources to our growing global engineering capabilities. They provide new technologies and position us with several market-leading products and solutions that expand and complement our current capabilities. They bring proven and established relationships and certifications to accelerate our expansion into important markets, including aerospace and defense, automation, robotics, life sciences, semiconductor and medical. And they expand our offerings and lead us into more demanding applications. Thus, our broadening capabilities enhances our value proposition and our competitive positioning. Ultimately, Allied is better positioned to create higher value solutions for our target markets and our customers.

In 2023, we expect the collective contribution of the six acquisitions to exceed $100 million in revenue with gross margins in the high 30% range and EBITDA margins in the high teens range. The purchase price of all six acquisitions, including future payments, was approximately $160 million and was made up of approximately 70% in cash and the remainder in AMOT stock. Based on our cash flow projections, we expect to delever over time in a manner that aligns with and is consistent with our historical performance.

We further believe the new acquisitions will provide Allied with significant new opportunities, and we are focused on integrating each into the global Allied platform. By doing so, our intent is to maximize the opportunities and realize the full potential of these margin-enhancing businesses.

While we have now provided additional color surrounding the six acquisitions, I will caution you that we will not be providing individual unit performance information in the future as we will focus on leveraging the full One Allied potential and opportunities.

And with that, let me turn it over to Mike for a more in-depth review of the financials. Mike?

Michael R. Leach: Thank you, Dick. As a reminder, our results include a partial quarter of contribution from the acquisitions noted on Slide 4, as ThinGap was completed on May 24, FPH on May 30, and Airex towards the end of the quarter on June 17. We also had the contributions from the fourth quarter 2021 acquisitions.

Starting on Slide 6, we provide some detail regarding our top line. Second quarter revenue increased 21% to $122.7 million, a record level, which reflected strong demand in the Industrial markets, as Dick discussed, and incremental sales from acquisitions. The unfavorable impact of exchange rate fluctuations on revenue was $5.2 million in the quarter. Excluding FX; revenue was up 26% and organic revenue growth was 10%.

The recent acquisitions contributed to the Aerospace & Defense growth as that market vertical doubled from a year ago. Partially offsetting were lower sales in the Vehicle market of 3%, largely due to broad supply chain challenges within commercial automotive, and Medical markets, which declined less than 1% due to the lapping of the strong prior-year period that was still benefiting from some pandemic-related sales.

Sales to U.S. customers were 58% of our total compared with 55% in last year's period, and the balance of sales were to customers primarily in Europe, Canada and Asia Pacific. The mix shift reflects the impact of our acquisitions that largely sell to the U.S. market.

Slide 7 shows the change in our revenue mix by market on a trailing 12-month basis. Sales to Industrial markets were up 39% and driven by the end markets noted on the slide. Vehicle markets were down 4% as strong truck, agricultural and construction vehicle demand was offset by the broad supply chain challenges in other market verticals. As noted, acquisitions contributed to the Aerospace & Defense growth in the quarter, which drove the TTM performance. The change in Medical markets on a TTM basis reflects similar pandemic-related comps as the second quarter.

As depicted on Slide 8, our gross profit was 32.4%, a record level and up 170 basis points from the year ago period. Higher volume, margin accretive acquisitions and selling price increases more than offset continued global supply chain disruptions, rising material and labor costs and noncash acquisition costs. As Dick noted, you can see the significant improvement over the sequential quarter.

Moving on to Slide 9. Second quarter operating income was $7.5 million, or 6.1% of sales, compared with $6.7 million, or 6.6%, in the year ago period. Operating costs and expenses as a percent of revenue were 26.3%, up 220 basis points. This increase was all attributable to our M&A activity with higher business development and amortization expenses as well as added engineering and development costs that we have not yet fully leveraged.

As we have stated, we anticipate growing our margins over the long term with the disciplined execution of our lean toolkit, AST, combined with leveraging higher volume and continuing to evolve as a systems provider.

On Slide 10, we present GAAP net income and adjusted net income along with our adjusted EBITDA results. Second quarter adjusted net income, which excludes business development costs and other nonrecurring items, was $5.7 million, or $0.36 per diluted share, compared with $4.8 million and $0.33 per diluted share in the second quarter of 2021.

The effective tax rate was 27% in the second quarter. We expect our income tax rate for the full year 2022 to be approximately 25% to 27% based on changes to geographic mix.

Adjusted EBITDA was $16.2 million, or 13.2% of revenue, which was up 100 basis points. We use adjusted EBITDA as an internal metric and believe it is useful in determining our progress and operating performance.

Slides 11 and 12 provide an overview of our balance sheet and cash flow. Total debt was approximately $229 million at quarter end. During the quarter, we used $44.8 million of cash to complete the three acquisitions; net of cash acquired, which was largely funded by debt.

The debt increase also reflects a new finance lease that was highlighted during the first quarter of 2022 for our manufacturing facility expansion in Germantown, Wisconsin to support continued growth.

At the end of the second quarter, debt, net of cash, was about $200 million, or 49.9% of net debt to capitalization, and our bank leverage ratio was approximately 3.7x.

We have historically demonstrated our ability to delever our balance sheet following acquisitions and is our expectation that we will continue the strategy to reload for future growth opportunities.

We generated $13.1 million net cash from operations during the quarter and utilized $3.9 million on capital investments, which largely focused on new customer projects. We expect our 2022 CapEx to range between $15 million and $20 million and to be focused on growth opportunities.

Inventory turns were 3x in the second quarter, consistent with our 2021 performance as our teams continue to manage our inventory to meet increasing customer demand, combat sourcing and lead time challenges. Our DSO increased slightly to 49 days in the quarter, largely due to timing.

With that, I'll now turn the call back over to Dick.

Richard S. Warzala: Thank you, Mike. Our backlog and bookings remained strong as highlighted on Slide 13. Orders were more than $139 million in the quarter, representing a book-to-bill ratio of 1.1x. This level also reflects a noted FX headwind of $6 million.

Our backlog hit another record, increasing 12% over the sequential first quarter and up 90% over the prior-year period to approximately $324 million. About 2/3 of the sequential increase in the quarter was from our acquired companies. The time to convert the majority of backlog to sales is within the next 9 months.

Turning to Slide 14. We remain positive on our outlook. To reiterate, we have been busy on the M&A front, having now completed six acquisitions over an eight-month period. We believe these are strategic additions to Allied. As previously mentioned, we have now added approximately $100 million annually of new business that will be fully realized in 2023 with a measurably higher margin profile. Equally important to the collective financial contributions, our overall technology offerings are enhanced, and our competitive positioning in target markets is strengthened.

As we look forward, we are excited to leverage our stronger competitive position across our targeted markets. Specifically, demand is expected to remain strong across our many Industrial end markets and in particular, industrial automation, oil and gas and material handling.

Over the short term, Vehicle demand is expected to be muted due to the continuation of supply chain constraints. However, we do see encouraging production demand later this year and into 2023. Medical markets have largely lapped the strong pandemic-related levels and should remain solid. And Aerospace & Defense should improve, especially with the recent acquisitions.

While headwinds remain, we are confident that we can continue to anticipate and make the necessary adjustments to mitigate potential impacts, and we remain highly confident in our ability to enhance both our top and bottom line performance in the future.

With that, operator, let's open the line for questions.

Greg Palm, *Craig-Hallum Capital Group*

Congrats on the good results here. So maybe starting with a broader macro view, what you are seeing thus far in July based on the quarter, based on the bookings, does it imply that you are seeing any slowdown? Any end markets, any geographies that maybe are a little bit more concerned versus last time we talked? Or is everything still fairly strong at this point?

Dick Warzala: The indicators are still quite positive in everything we have seen so far. Given it is summer in Europe, we do expect to see some slowdowns in business and potentially, of course, there are FX headwinds and potentially the impacts of the Ukraine war. But right now, we have to say that things seem to be continuing and are still strong.

Greg Palm: And gross margin, which was clearly the bright spot. How much of the improvement are you able to quantify from the acquisitions alone in the quarter knowing that those are higher-margin contributors? And then can you also quantify the impact from what you are still seeing from the supply chain challenges. Did that get any better this quarter?

Dick Warzala: Let's start with the supply chain. We are seeing some slight improvements. And when I say slight improvements, some lead times are starting to shorten, and we are getting some pleasant surprises of things showing up that were expected.

On the other side, there is still the negative surprises that are occurring. Our teams are still fighting the battle, and it's those couple of components that may be missing that prevent you from shipping your products. Those are the battles that we continue to fight every day. Some are doing better than others. Electronic components are still a challenge; although, we are starting to see some light at the end of the tunnel here.

As far as the contribution of the acquisitions versus the core business, let's call it, clearly, the acquisitions, as we mentioned, the margin profile is higher, and it did have an impact.

Though, we have seen some improvement in our core technology units, as we call them, our business units. I think it's really a testament to our team who continues to focus on where the inefficiencies exist because of material shortages and an inability to build complete products. Some of that is starting to go away, and we are starting to see some improvements.

We have done a facility consolidation, and that has gone quite well. We have also shifted some product lines around during the quarter which has gone quite well. Overall, I see the operating team doing an excellent job in working with what they have, and it is a positive impact. The majority of the impact for the margin increase clearly comes from the higher-margin generating businesses. Now remember, they were in the quarter. They were near the end of the quarter when they occurred from a percentage standpoint that clearly were higher.

Mike Leach: I would concur and add that the collective six acquisitions delivered as expected from a margin perspective. I think we said collectively in the past that they would largely deliver our goal of the 100 basis point improvement in margin.

The other item that I would highlight is we talked previously about the lag in selling price increases on a contractual basis. And certainly, that lag caught up here in Q2, in terms of them being passed through both on a contractual basis and significantly on a negotiated basis, to fight the elevated input costs. So I think that was another strong comp contributor to the quarter, besides the acquisition, was our success in passing along those selling price increases and neutralizing, if you will, to some extent, the supply chain impact.

Greg Palm: That's helpful. So if I think about the go forward, you will now have a full run rate contribution from the higher-margin acquisitions. Then if you assume that supply chains continue to improve, it would seem logical that what you saw in Q2 can probably be improved upon in future quarters. Any reason why that wouldn't be the case?

Dick Warzala: It does make sense for us to be able to do that. We would caution you that we do have one of the acquisitions that is still lagging and not contributing to the levels that we had initially planned, but we see it moving to the right.

The backlog is very strong, but that has been impacted by the supply chain and electronic components, so we're not realizing the full impact of that. It's questionable whether that will even resolve itself in the third quarter. So I would just caution there is some muting going on there, but overall, what you have stated, Greg, I think, is fairly accurate.

Mike Leach: I think that impact, as Dick described, is more so on the operating margin side than the gross margin side, but it does impact gross margin to some extent.

Greg Palm: Got it. Then last one, just without getting into specific customer names, can you give us some sense of what end markets you are seeing the most traction for in terms of these new wins; what types of applications or solutions you are seeing the most progress in?

Dick Warzala: It is kind of interesting. What we are seeing here is across the board, which I think speaks well to our diversification. We are seeing some specialty vehicle because our solutions are quite special in those applications. We are seeing industrial opportunities, medical opportunities and defense opportunities.

I would just have to say to you that is the exciting part about it. It is not just one vertical; we created this platform. We created this subset of markets that we feel are growth opportunities. HVAC still is strong. Oil and gas, of course, has been strong. So it is across the board. Our solution offerings are having an impact there.

Gerry Sweeney, *ROTH Capital Partners*

Dick, you had mentioned one of the acquisitions is still evolving to where you want to get it. I suspect that with Spectrum Controls, and I know you do not necessarily call out business units, as you said earlier, but that Spectrum was one that you did say was going to be a little bit slow in terms of hitting targets just because of some supply chain issues. Am I correct in that assumption?

Dick Warzala: I am not going to deny that, and it is largely due to supply chain issues.

Gerry Sweeney: The follow-up to that is obviously still very bullish on the technology it brings to the team.

Dick Warzala: Absolutely. The backlog is strong and it is interesting. There are a few components here or there that are preventing us from really getting the full production rate out the door. I would say to you, Gerry and everyone else, is that even without that, we performed fairly well. We are not clicking on all cylinders yet. That is a good part to look forward to in the future when it kicks in, it will definitely improve even where we are today.

Gerry Sweeney: Just from a solution standpoint, since we're on it. I mean the whole idea of one of the key themes, I believe at Allied Motion, was to shift more from component sales to solution sales. I mean, obviously, I think these acquisitions probably help in that manner. But should we, at some point, even look at component sales going completely in the rearview mirror and you become a total solutions provider and that helps margins? Or will there always be a mix in there?

Dick Warzala: Great question. I think the best way to answer that is to point you to a slide here and look at a similar slide in prior years to the system solutions that we are offering today.

I'll point you to Slide 5 for anyone that has the presentation. It is what we called the solution in the past, if you look at the first product that is shown on the left. The automated GPS-guided vehicle steering module is a motor with embedded electronics and connectors and cabling. That was the bulk of the Allied system solution offering; something that would look like it would be embedded; you would have electronics and/or gearing embedded.

What I will say to you in the future, and we have talked about this internally is that is becoming part of our culture; that it is going to be the exception when we are shipping components, let's just call it a motor, and it is going to be more about the motor and the electronics and/or the gearing, which we use. We call it a solution, a relatively lower level solution, compared with the rest of the pictures that you are seeing here on that same slide.

That system solution, let me just throw numbers out, without giving out too much information, with a motor and electronics, we are talking in the range of an ASP of anywhere from $100 to $500 or $600. When you start getting into the other solutions that we are showing you here, you are talking about tens of thousands of dollars and even hundreds of thousands of dollars. They do embed all the components that we offer, but they are bringing it at a higher sophistication level, with much more software involved.

I would tell you that as we look out into the future that is what you are going to see. You are going to see more embedded software, more informatics, more Allied transitioning into a solution provider that can do model-based design and simulations and very precise high-level solution packages that are with ASPs that are much higher. We will not abandon that core component ability to produce product at a competitive price anywhere in the world. We feel that is core to our future technology, and we will not abandon that because we can leverage that into our other markets, and we continue to do that. It gives us that core unifying we need, but it is the magnitude of what is in there.

There is still, even in those motor and electronic solutions, a tremendous amount of software, and it just continues to develop and evolve and is very sophisticated.

This is a good picture of transitioning what we call solutions, and the past is changing. It is getting to a much higher level, including much more embedded software, much more communications capabilities. Then the components of the past, with more IP, will be components rather than systems.

Gerry Sweeney: I have a couple of other questions, but I want to save them for a follow-up call, but I appreciate it and congrats on a really great quarter.

Dick Warzala: Thank you, Gerry.

Mike Leach: Thank you.

Operator: This concludes the question-and-answer session. I would like to turn the conference back over to management for any closing remarks.

Dick Warzala: Thank you, operator, and thank you, everyone, for joining us on today's call and for your interest in Allied Motion. As always, please feel free to reach out to us at any time and we look forward to talking with all of you again after our third quarter 2022 results. Thank you for your participation and have a great day.

Note: This transcript has been edited slightly to make it more readable. It is not intended to be a verbatim recreation of the Allied Motion (AMOT) financial results teleconference and webcast that occurred on the date noted. Please refer to the webcast version of the call, which is available on the Company's website (www.alliedmotion.com), as well as to information available on the SEC's website (https://www.sec.gov/) before making an investment decision. Please also refer to the opening remarks of this call for AMOT's announcement concerning forward-looking statements that were made during this call.