Operator: Good day and welcome to the Allient Incorporated Fourth Quarter Fiscal Year 2023 Financial Results Conference Call. All participants will be in a listen-only mode. [Operator Instructions] After today's presentation, there will be an opportunity to ask questions. [Operator Instructions] Please note this event is being recorded.

I would now like to turn the conference over to Mr. Craig Mychajluk of Investor Relations. Please go ahead, sir.

Craig Mychajluk: Thank you and good morning, everyone. Here 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 fourth quarter and full year 2023 results, and provide an update on the company's strategic progress and outlook, after which, we'll open 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 allient.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 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, 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 will 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 will turn it over to Dick to begin.

Dick Warzala: Thank you, Craig, and welcome, everyone.

With a backdrop of macro uncertainty and other challenges, the Allient team once again delivered on a number of successes during the past year.

This included the kickoff of our next stage of growth with a refined strategy that brought on a new corporate name and ticker, and included the publishing of our inaugural sustainability report, which highlights our vision for and approach to corporate sustainability.

We continued to execute our financial strategy with the support of 13% organic growth for the year, which is more than double the industry, and key acquisitions which I will speak to in a moment. Our top-line reached nearly $580 million, reflecting strong demand in Industrial markets, largely driven by industrial automation projects and power quality solutions focused on the HVAC and oil & gas end markets. Also contributing to our overall growth was higher sales within Aerospace & Defense and Vehicle markets.

On the margin front, we delivered on our expectations with a record annual gross margin of 31.7% and operating margin of 7.3%, which was up 100 basis points for the year. This translated into stronger earnings that also led to a record level of cash generation of $45 million that enabled us to reduce our debt while still investing in organic and inorganic initiatives.

Overall, annual net income per diluted share increased 36% to $1.48 and on an adjusted basis, net income per share was $2.30, up 22% for the year.

On **slide 4** we highlighted our recent acquisitions. We reviewed Sierramotion on our last earnings call as we completed the transaction in September. While it is a relatively small acquisition, it was very strategic from an engineering perspective as it enhances both our application design and development efforts in support of our integrated motion solutions strategy, and advances our customer facing market strategy as we further expand our reach into our targeted end markets segments.

In early January, after the year closed, we brought on SNC Manufacturing, which was our first tuck in acquisition in support of our Power technology pillar. They are a well-established company with locations in the U.S., Mexico and China. Their offerings are complementary to our current power quality capabilities as they design and manufacture electromagnetic products for blue-chip customers in defense, industrial automation, alternative power generation and energy, which includes electric utilities and renewable energy. In addition to extending our capabilities in the clean power industry, SNC brings much needed incremental, low-cost manufacturing capacity and expertise to further grow our power quality business.

From a financial perspective, SNC adds about $40 million of annual revenue and is expected to be accretive to earnings in year one. While their current margins are less than our stated goals, we are very confident that we are well positioned to improve them over time. In addition, we see several opportunities to leverage the resources within the Power Pillar and Allient as a whole, and to have a positive impact on sales and profits in the short term as well. We welcome all employees of SNC to Allient and we look forward to continued growth and success together in the future.

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

Mike Leach: Thank you, Dick. Starting on **Slide 5**, we highlight our top line for the quarter and full year periods. Fourth quarter revenue increased 8%, or nearly $10 million, to $141 million. Excluding the favorable impact of foreign currency exchange rate fluctuations on revenue of $1.6 million, organic growth was approximately 6%.

Industrial markets were up 23% in the quarter, benefiting from strong end market demand within industrial automation, vehicle handling, and power quality solutions focused on the oil & gas, and HVAC markets.

Within our Vehicle markets our automotive customers began to ramp up their programs as expected this past year and we also saw nice demand from powersports which helped drive the overall vertical up 17% in the quarter. Offsetting some of that growth continued to be lower demand within agricultural vehicles given the softness in Europe, which was largely influenced by the Ukrainian conflict.

A&D sales were down just given the timing and resulting lumpiness around certain defense and space projects along with customer driven supply chain challenges within the vertical. Medical markets declined due to softness in medical mobility, which largely reflected a reduction in the demand that we experienced during the last few years for those products.

Slide 6 provides some details regarding our full year performance and shows the change in our revenue mix and the drivers behind each change. Industrial continues to lead the way and remains our largest market, making up 44% of total 2023 sales. That's an increase of 600 basis points since 2022. The 33% growth in the Industrial space was primarily driven by the same markets as the fourth quarter, and reflected continued improvements within the supply chain environment, which supported the shipping of some long lead projects.

The A&D vertical is better evaluated on an annual basis given program timing and for the year we grew low double-digits due to the successes winning new defense programs and the ramping of other programs. We also benefited from positive commercial aircraft demand given overall improvements within the industry.

Vehicle market revenue was up 2% and reflected the same demand drivers as the fourth quarter.

Medical sales were nearly flat as we continued to see a return to a more normalized sales environment focused on surgical and instrumentation-related end markets.

And lastly, sales through the Distribution channel, which are a small component of total sales, were up 6% for the year.

As highlighted on **Slide 7**, gross margin expanded 40 basis points for the quarter and full year period on higher volume and favorable mix, along with the continued emphasis and usage of our lean tool kit throughout the organization. These impacts more than offset elevated raw material costs and remaining supply chain inefficiencies.

Moving to **slide 8** for our operating performance, you will notice we had a sizable increase in business development costs for the quarter and full year period. Those expenses were in support of the recent acquisitions, an earnout for a prior acquisition and some rationalization efforts around our manufacturing footprint to position us to drive stronger operating leverage in the future.

On an annual basis, we did gain some operating leverage which drove operating income growth of 34% to $42.3 million, or 7.3% of sales, up 100 basis points.

On **Slide 9**, we present GAAP net income and adjusted net income, which we believe provides a better understanding of our earnings power, inclusive of adjusting for the noncash amortization of intangible assets, which reflects the company's strategy to grow through acquisitions as well as organically.

Fourth quarter net income increased 18% to $4.3 million, or $0.26 per diluted share, and on an adjusted basis, was up 31% to $9.1 million, or $0.55 per diluted share. Included in the fourth quarter's results was a tax benefit of $0.4 million, which reflected realization of certain NOLs and R&D credits and incentives.

For the full year, net income increased 39% to $24.1 million, or $1.48 per diluted share. On an adjusted basis, annual net income increased 25% to $37.5 million or $2.30 per diluted share.

The effective tax rate was 18.9% in 2023, which reflected the tax benefit from the fourth quarter due to realization of certain NOLs and R&D credits. This compared with an effective tax rate of 26.6% during 2022. We expect our income tax rate for the full year 2024 to be approximately 21% to 23%.

We use adjusted EBITDA as an internal metric and believe it is useful in determining our progress and operating performance. Adjusted EBITDA increased 2% to $16.9 million, or 12.0% of revenue. For the year, adjusted EBITDA increased 18% to $77.2 million or 13.3% of revenue, which was up 30 basis points.

Slides 10 and 11 provide an overview of our cash flow and balance sheet. We generated $45.0 million of cash from operations for the year, which represented a record level for the company and a significant increase from the $5.6 million generated during the prior-year period. The increase reflected higher net income and improved working capital management. Based on our cash flow projections, we expect to continue to drive strong cash flows, consistent with historical trends.

Annual capital expenditures were $11.6 million and largely focused on new customer projects. We expect 2024 capital expenditures to increase from this level and be in the range of $16 million to $20 million.

Inventory turns improved to 3.0x compared with under 3x last year. Our DSO was slightly elevated at 56 days for the year, largely reflecting timing and mix of customers.

Total debt was approximately $218 million, down $17.1 million from year-end 2022. Debt, net of cash, was about $187 million or 42.6% of net debt to capitalization. Our bank leverage ratio was 2.8x.

Lastly, we recently extended the maturity of our existing $280 million revolving credit facility for five years to 2029. Borrowings for the revolving facility will bear interest on a sliding-scale rate based on leverage of 1.25% to 2.50% over SOFR. In addition, for added flexibility, we entered into a $150 million fixed-rate private shelf facility with PGIM. The notes will have a maturity date of no more than 10.5 years after the date of original issuance and may be issued through March 2027. Currently, there are no borrowings under this agreement.

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

Dick Warzala: Thank you, Mike. **Slide 12** shows our orders and backlog levels.

As we have discussed throughout the year, the change in backlog reflects the continued improvements within the supply chain environment, which has enabled the shipping of some long lead industrial market focused projects and led to customer order patterns returning to a pre COVID-19 environment.

There are a number of exciting programs that will begin to play out as we move through 2024 and we are well situated as we realign the organization to support the significant opportunities that we are bidding across our targeted verticals.

The upcoming year will have its challenges given the changing dynamics of our backlog, which is expected to continue to right-size for at least the next few quarters. This also presents the opportunity to reduce our working capital requirements and strengthen cash flow.

Turning to **Slide 13.** We are intent upon creating stronger earnings power with our *Simplify to Accelerate* strategy. 2024 is the year to drive out redundant costs, realign the organization to improve focus and efficiencies, rationalize our footprint, and ultimately simplify our operating structure.

By rethinking how we operate, we believe we can accelerate our efforts to achieve top-tier financial performance. While some of the actions will take time to fully execute, there is a strong sense of urgency throughout the organization to deliver on our goals.

Our *Simplify to Accelerate* strategy is moving forward by adding the word now to the end and is centered on three high level strategic initiatives:

1. First, Realigning and right-sizing our footprint to better align with our markets and customers. Initiatives began in 2023 and are expected to continue with earnest throughout 2024 and beyond.
2. Reinforcing lean principles throughout the company to accelerate margin expansion. Our AST toolkit is core to the continuous improvement actions required within the company.
3. And, as we demonstrated this past year, we expect to continue to employ working capital initiatives and strong financial discipline to drive additional cash generation and de-lever the balance sheet in 2024.

Overall, we are excited and confident in our future as we believe we are well positioned to drive our earnings power with our *Simplify to Accelerate Now* strategy and create additional value for all of our stakeholders.

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

Question & Answer

Operator: Thank you. We will now begin the question-and-answer session. [Operator Instructions] And at this time, we'll pause momentarily to assemble our roster. And the first question will come from Greg Palm with Craig-Hallum Capital Group. Please go ahead, sir.

Danny Eggerichs: Thanks. This is Danny Eggerichs on for Greg today. Congrats on the good results, guys.

I think I'd like to just kind of start out by maybe what you're seeing out there right now, any quarter to date trends. Obviously, bookings kind of fell off a little bit in Q4. You noted some inventory drawdown. So maybe just what kind of visibility do you have into this? Are trends, have they kind of continue to off those Q4 levels and maybe how long do you think some of those some of those trends should last for? Thanks.

Dick Warzala: Sure. Thanks. Well, I would say this you that, as we mentioned, we expect that over the next few quarters here we're going to continue to see some adjustments. And it's a mixed bag. While we have seen, the hold on shipments or the delay of shipments, so the inventories do get balanced properly at our customer level. We're also starting to see that where it was projected for certain demand to be pushed out, starting to now see some demand increasing in the near state, in the near time frame. So, I think it's as I said, it's a mixed bag. We overall believe that the lead time adjustments, the lead times reductions and a better management of inventories throughout the whole supply chain, including our own, are certainly actions that are at the top of our list and as well as our customers. And that the next few quarters will see some continued adjustment there. That's our expectation.

Danny Eggerichs: Got it. That's helpful. Maybe just dig in a little bit more into this Simplify to Accelerate initiative. Any more color you could give there. What are you doing? Is there headcount reductions as part of that? Maybe like a why now do you think we'll see this in gross margin or OpEx, how to break that out? And I guess any way you can kind of quantify those impacts to the P&L as we move throughout the year?

Dick Warzala: Yes, sure. I would just as a last statement in my prepared remarks. So, we said the Simplify to Accelerate strategy, which actually started last year and is gaining momentum within the company, but we added a very important word to the end of that. That's now and it's not the future, it's now. And I can't stress that enough to say that in everything we do and as we start to look at all processes and operations and capacity and within the company, you could see complexity that needs to come out. So, what I would say to you is that we had defined some activities and some actions and that were pre-COVID that we would have undertaken.

But given COVID, those resources were diverted into other directions, simply making sure we could get parts, satisfying customer demand, working overtime, getting the workforce in place and so forth. I would just say that they have been delayed. Last year when we had our strategy session with our key leadership team, we absolutely said it's time now to get back on to those initiatives and wring some cost out of our operations. So, what you mentioned, I would say, is all of the above. Nothing is sacred at this point. We did eight acquisitions in a very short period of time. We know we can do a better job of leveraging the capabilities and the footprint to these acquisitions and bring teams together.

We've got brands out there that need to be retired. We've got company names that need to be retired. As we move forward to the one company image, we launched the new name last year with a new ticker, and it's purposeful. I mean, we really have a unique situation with technology and products that we could leverage into target verticals. So, with further expansion and acceleration of those activities, and a focus on making those things happen. So, it really is an opportunity for us to look at how we're doing business, use our Lean Toolkit to help us on continuous improvement. And as I said, it's now, it's not planning for the future. We have actions that our plan that we will execute and move forward on and our leadership team is engaged. So they will obviously the goal here is to improve. We make commitments to improving margins. This will absolutely help us achieve those goals.

Danny Eggerichs: Yes. So, you kind of said there that I guess 100 basis points of annual gross margin improvement target that you have out there. Does this new initiative work towards that, or do you think you can get incremental expansion on top of that with this? How should we think about that?

Dick Warzala: Yes, well, I think listen, first off, we, it's hard to adjust expectations or statements that have been made in a couple of years ago. We wanted to realign what the expectations are as far as 100 basis points of margin improvement, including gross margin with our expectation, 50 basis points for both gross and from the operating expense side of it. But let's make sure that that's clear.

Our goal internally is to exceed what we state as public goals. This is not in addition to or anything different than when we laid out our expectations for the improvements a few years ago. This is lining right up with what we stated back then. So, while in the process we see opportunities to do better, we absolutely will, of course. But I think we'll stick with our stated objectives here for the 100 basis points improvement in operating margin, with a combination of both gross and operating expense reduction.

And one of the things I'll bring it up, I think that you even asked the question before, is that as we did all the acquisitions, you could see revenue line going up, but you also saw the SG&A expenses going up along with that? That is correct. And at some point, you have to leverage those increased costs to either grow revenues, earnings some more, or to find ways where you can realize some synergies. That percentage reduction should go down. You should actually see synergies there and start to leverage that.

Danny Eggerichs: All right. That's helpful. I'll leave it there. Thanks.

Operator: The next question will come from Gerry Sweeney with Roth Capital. Please go ahead.

Gerry Sweeney: Dick, Mike, thanks for taking my call. Mike, I think this is your last call, so congratulations.

Dick Warzala: It's his last call. Oh, come on. Come on Gerry. That's Gerry, too by the way. Not Gerry. Right?

Gerry Sweeney: No worries anyhow I know we covered the Simplify to Accelerate, so I'm going to let that be for now. Have some follow-ups on that later today. But A&D, just some random questions here, is obviously lumpy. We've always talked about that. But just curious, look at that on an annual basis, how much confidence you have will say throughout 2024 that, it sounds as though there are some programs that are out there, and you feel relatively confident that the business is well positioned.

Dick Warzala: Yes, well, absolutely. I think we've mentioned over several conference calls that the quoting activity has been extremely high. That didn't necessarily convert into orders, which was a little bit of a surprise. But we have seen the orders now coming in and as to our expectations that that are replenishment of certain materials that's needed by the defense markets. So, we do have visibility on programs beginning to kick in and starting to accelerate mid-year and through the end of the year and in some fairly significant programs out into the future.

So, it is it is beginning to kick in and I will state that it is our first, what we would really say internally, we call it the Allient market specific selling unit where we want to realize as much value as possible in these in that market. We are backing it up by putting resources in place and having a strong focus on it. And I just mentioned we just finished up a global leadership meeting here last week and you see the excitement as we bring our team together, how much we really do from an independent unit standpoint and how much we can leverage when we bring a focus to it and have a central point of sale and contact support of the continued increase in value in a sale that we will see.

Part of that process also, as we talk about and Danny asked the question earlier to some of the initiatives, but I would say specifically, how we process, how we handle orders. We the acquisitions that we've done, we have different computer systems, and the transactional costs are quite high because of the way it's being handled. And our whole goal is to simplify it, to make one transaction, drive it all the way through the system, have it happen automatically, and to realign revenues and profits into the right units who are contributing.

Sounds simple, sounds trivial, but as the organization has grown one of the things I wanted to be very cautious of when you we hear this many times as big companies become cumbersome and they don't want to do business with their sister companies, we have to make sure that we do things differently and we prevent that from occurring. And we could see it creeping in and we think we've got a pretty good solution. And in the process, we're going to have a much better focus. So, we're going to drive cost out as well as aligning more from a system sale. We think there's a lot of positives there. This will be moving forward this year, and it is a strong focus and it's based upon the demand that we're actually seeing in the market.

Mike Leach: Just add on to that Gerry. During my prepared remarks, I mentioned some supply chain inefficiencies within A&D. There are suppliers to our customers that are holding up release, if you will, of our products because they, they're not in a position to produce their full capacity. And obviously, they're holding off on delivery of our products so that we can marry that together for a full system. So, we are being impacted by that. We are excited about the programs that we previously discussed. Like I said, some of that is being held a little hostage to certain supply chain constraints within that vertical.

Gerry Sweeney: Got you. Taking a half a step back. Going back to you, Dick, the Simplify to Accelerate, it sounded as though there is an opportunity not just for cost savings but for we'll see wild share getting, a larger solution into a customer and getting some of the, acquired businesses to, for lack of a better term, interact with, the mothership per se. Right. Is that a fair assessment?

Dick Warzala: Absolutely. And again, just use examples of in our business, one of the primary objectives, if you want to win in this business is be first to market with the solution or to the customer with a solution. In a complex system, does nothing but drag you down and delay the process of getting to the customer with solution. So, in addition to adding efficiencies, looking at increased value in the sale, it's looking at more efficient solutions for the customer at a larger scale, it is shortening the time to market from the time to make contact, but to the time that we present a solution to them, we want to be first, we need to be first and being first, you will increase the top line.

Gerry Sweeney: Got it. That makes sense. That's right. So, acquisitions, right. Do you slow down acquisitions at this point? Is this sort of like, hey, made eight acquisitions in the last couple of years?

Dick Warzala: We need to do more work on making sure that everything that we've acquired is functioning and performing as expected. We have the most recent acquisition at SNC. We were very excited about that. I mean, the off of this, the synergies that we see already and the opportunities there to leverage, they just happened to see that TCI or company up in Germantown, Wisconsin, and SNC and Oshkosh are very close.

They're complementary; They're working extremely well as a team right now. And we're starting to leverage resources already for both organizations, which is very exciting. And I do think that the emphasis needs to be on that. Now We're still grooming. And if the opportunity came for something, we can't look the other way. We'll still pursue. But it's really more of an emphasis to answer your question on making sure we're making what we have work better.

Gerry Sweeney: Got it. So, we're sort of, quintessentially make some acquisitions, take a step back, optimize drive cash flow that's going to start coming down. And then in the background, there's still some acquisition opportunities, but they'll be accelerated as you go through.

Dick Warzala: Exactly.

Gerry Sweeney: Okay. That's it for me. I know we have a follow up later, so I appreciate it. Thank you.

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

Dick Warzala: Thank you, everyone, for joining us on today's call and your continued interest in Allient. We will be participating in the Roth conference on March 18 in Dana Point, California. Otherwise, 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 first quarter 2024 results. Thank you for your participation and have a great day.

Operator: The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.

Note: This transcript has been edited slightly to make it more readable. It is not intended to be a verbatim recreation of the Allient, Inc. (ALNT) 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.allient.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 ALNT's announcement concerning forward-looking statements that were made during this call.