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IDEX Corp. (IEX)

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MANAGEMENT DISCUSSION SECTION

Operator: Greetings and welcome to the IDEX Corporation Third Quarter 2016 Earnings Conference Call.

At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. [Operator Instructions] As a reminder, this conference is being recorded.

I would now like to turn the conference over to your host, Mr. Michael Yates, Vice President, Chief Financial Officer, and Chief Accounting Officer for IDEX Corporation. Thank you. You may begin.

Michael J. Yates

Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

Thank you, Melissa. Good morning, everyone. This is Mike Yates, Vice President and Chief Accounting Officer and Interim Chief Financial Officer for IDEX Corporation.

Thank you for joining us for a discussion of the IDEX third quarter financial highlights. Last night, we issued a press release outlining our company's financial and operating performance for the three-month period ending September 30, 2016. The press release, along with the presentation slides to be used during today's webcast, can be accessed on our company's website at www.idexcorp.com.

Joining me today is Andy Silvernail, our Chairman and CEO.

The format for our call today is as follows. We will begin with Andy providing an overview of the third quarter financial results. He will then provide an update on our markets and geographies and discuss our capital deployment. He will then walk you through the operating performance within each of our segments for the third quarter. And finally, we will wrap up with our outlook for the fourth quarter and full-year 2016. Following our prepared remarks, we'll then open the call for your questions.

If you should need to exit the call for any reason, you may access a complete replay beginning approximately two hours after the call concludes by dialing the toll-free number 877-660-6853 and entering the conference ID 13620008, or you simply may log on to our company's homepage for the webcast replay.

As we begin, a brief reminder. This call may contain certain forward-looking statements that are subject to the Safe Harbor language in today's press release and in IDEX's filings with the Securities and Exchange Commission.

With that, I'll turn the call over to our Chairman and CEO, Andy Silvernail.

Andrew K. Silvernail

Chairman and Chief Executive Officer, IDEX Corp.

Thanks, Mike. Hey, I appreciate everybody joining us here for our third quarter conference call. As we get into the details here, I wanted to lay out a couple of very important messages.

In the face of continuing macroeconomic challenges, I think there are three critical things to take away. The first is our execution has been outstanding. Whether it's profit execution or cash execution or focusing on our critical niche markets and our profit pools, our teams have done really an exceptional job around that. Second, I think we can note the power of our disciplined capital deployment, and I'll go into that in detail as we walk through the call here.

And three, we are extremely well-positioned with our balance sheet and our cash flows to continue with our disciplined capital deployment to drive total shareholder return. And so as we go through the discussion today, I think those are the three key messages to keep in mind.

In the quarter, we saw a ratable uptick in orders throughout the quarter as we did in the second quarter. We delivered 2% organic growth; I mean, that's the first time we've seen that in six quarters. And overall, the results were strong. Our orders were up 9%. Our sales were up 5%. Again, organic orders were up 2%. Organic sales were down 2%.

We had adjusted EPS of $0.92, which was up $0.03 or 3%. But please keep in mind, that included a $4.6 million inventory step-up charge related to AWG and the SFC acquisitions.

Our adjusted operating margin was 20.9%. That was down 60 basis points from last year, but it was negatively impacted by that step-up that I just noted of $4.6 million. In the fourth quarter, we're going to have a remaining $5.2 million of step-up for the SFC acquisition, and I'll go through that in more detail. But I think it's important to note that in the quarter, we saw an impact of about $0.04 a share in step-up, and it impacted our operating margin by 90 basis points.

In the quarter, we had tremendous cash production, $125 million of operating cash production and $114 million of free cash flow, which I'll note is a record. We did close the two acquisitions in the quarter, AWG and SFC. AWG was on July 1 and SFC was on August 31. And we're delighted to have both of them as part of the IDEX family, and I'll talk a minute more about how they fit and our outlook for those businesses.

Additionally, we divested two non-strategic product lines in the quarter, and we did a third here in the first part of October. We also made the decision to utilize $125 million of our overseas cash to partially fund the acquisitions. That did come at a cost of about $5.2 million in the quarter, and it raised our effective tax rate to 29.6% versus our guidance of 27%. That had a $0.03 negative impact on our adjusted EPS for the quarter.

And again, I'm going to – in just a few minutes, I'm going to take some time and walk you through the puts and takes so you can get a clean sense of what our operating earnings were for the quarter and what you should expect going forward.

Before I do that, however, let me talk a little bit about what we're seeing in our core markets and geographies. Really, the trends remain the same from what we've been talking about for the last three quarters or so. In our energy world, demand does remain weak. It impacts our energy, our BAND-IT and the Sealing solutions platforms. But it's certainly no worse than we've seen at any one time, and then we've talked about stability in some of those markets.

And that, that goes true for our industrial world especially in industrial distribution. We have seen stability. We talked about that in the second quarter and we've seen sequential stability from Q1 until today and certainly in our day rate business.

On the ag side, ag prices continue to be depressed. We did see a little bit upside here in the quarter for the first time in quite some time. And although we're certainly not calling an improvement here, we do believe that we've seen it bottoming.

Life science and Scientific Fluidics continues to outperform. This has been a great story for us for quite some time and it will be going forward. Our core markets of bio, analytical, instrumentation and IVD are all doing well.

With that said, there has been some news lately about what's going in the genetic sequencing world. So I wanted to take a second and just address that.

First and foremost, that is a great segment of the market that's going to grow double-digit for the foreseeable future and it's going to have legs for a long time to come. And so we like our position in that market. We like our – where we're positioned with customers in that market. But also remember, we don't have a single customer within IDEX that represents more than 2% of our sales. And so there has been some – we've seen some commentary lately suggesting that it's substantially higher than that, but I just wanted to make sure that we were accurate, that no customer represents more than 2% of our sales. We are bullish about these markets as we go forward and we'll continue to make bets aligned with those markets.

Municipal, it remains solid and we do expect to see modest increases going forward as we've noted in the past discussions.

Around certain regions, North America, the story here is really around what's happening around industrial and energy markets principally around industrial distribution and we expect that to be, as I've just mentioned a minute ago, stable, but, really, no signs yet of recovery.

Europe, obviously, with what's going on in the UK, it brings some volatility. We haven't seen any direct impact to our business, and Europe has been positive for us this year, especially around our dispensing and our water businesses.

In China – or Asia rather, China has been muted, and India has been a very good news story for us, especially around our fire, our rescue, our energy, and our dispensing businesses.

All right. Let me pivot for a moment and move from markets to talk about capital deployment because that's been a big piece of our story here in 2015 and now 2016. If you think about our value-creation model, it's very much supported by balanced and disciplined capital deployment strategy. And we're going to fully fund organic growth. We've always made a commitment to do that, and we'll continue to do that. We're going to pay consistent shareholder dividends. We'll buy back shares when it makes sense to create value. And we are going to focus on executing in M&A. We've got a great balance sheet, strong free cash flows, and a good acquisition pipeline as we think about the balance of 2016, and certainly into the future.

On M&A, we've put over $0.5 billion to work here this year, including AWG, SFC, and also Akron earlier in the year. If you think about AWG and Akron in particular, it helped us build a terrific fire and safety platform. We have channel opportunities. We have innovation opportunities. And we certainly have cost opportunities to drive this portfolio into the future.

We also completed the acquisition of SFC KOENIG on August 31. That cost us €217 million, and we've got a great business here based in Switzerland. They're global leader around highly-engineered metal-to-metal seals. It really focuses on high pressure and high temperature and transportation to hydraulic markets, but it's very scalable. As I think about opportunities in their core business to take market share and in adjacent businesses around aerospace and medical, we have a terrific business in SFC, and we're delighted to have all three as part of the IDEX family.

Other elements of capital deployment. This year, we've spent $55 million buying back 739,000 shares at an average price of $74 a share. And so I think we've executed that well. As I mentioned before, we're going to fully-fund organic growth. We've taken an aggressive segmentation to our portfolio thinking about where we have great advantages and niches and where the profit pools are really attractive, and we continue to drive investment in that for above-market growth.

And then finally on dividends, we have told you for a long time now, our goal is 30% to 35% of net income, and we'll continue to execute around that.

The last element I want to talk about with capital deployment is really the position of our balance sheet, and I think this is critical as you think about our ability to drive total shareholder return for the long-term.

As I noted earlier, we utilized $125 million of our global cash to fund our Q3 acquisitions. This did drive a higher-than-expected quarterly tax rate, but we thought it was prudent given where the cash sat around the world, our ability to put money to work at an attractive return versus sitting idle.

And I think it's important to note that our long-term debt balance increased only $45 million when you compare September 30 to June 30, even while we invested $288 million of capital into AWG and SFC in the third quarter. And so we sit today at only around 2 times leverage on a gross EBITDA basis, and we've got plenty of capital availability.

We've got $450 million of revolver. And if you think about the last three years, we've averaged about $335 million of free cash flow. And we've got $240 million still sitting on our balance sheet. So, as we think about our ability in the next three years to deploy $1 billion of capital, I feel very comfortable that we're able to do that.

As I've mentioned before, we have divested three product lines in 2016. Two of those happened in the third quarter and one just at the beginning of the fourth quarter. And this is really an emphasis around optimizing our portfolio. We've talked a little bit about this in the future. These are not big businesses nor do we expect to divest large chunks of business, but we do want to always think about positioning our product portfolio as we go forward.

I think it's important to note, if you take the acquisitions that we've done and the small divestitures that we've done, I want you to think about the impact that we expect going forward into 2017. The bottom line is that we expect about $0.25 of incremental earnings in 2017 from the combination of our acquisitions minus the small impact of divestitures. So again, $0.25 of incremental impact in 2017 compared to 2016.

All right. With that, let's move to slide four and we'll start to talk about the results, and then I'll get into the segments. So in the third quarter, we had – orders were $530 million, up 9%, 2% organically. And again, that was the first improvement we've seen since the first quarter of 2015.

Revenue was also $530 million; that was up 5%, but down 2% organically. And then operating margin for the quarter was at 20.5%. However, as I've mentioned before, it's at 20.9% when you think about the net loss and the divestitures, and that was down 60 basis points year-over-year. But it was due to a 90 basis points of pressure from the fair value inventory step-up that I walked you through earlier.

Cash flow again was a great story, $125 million cash from operations, $114 million of free cash flow. That was 163% of net income, and that was up $9 million or 9% from last year. Net income was $70 million. That delivered GAAP EPS of $0.91. If you take into account the loss from the divestures, adjusted EPS of $0.92, again up $0.03 or up 3% from last year.

All right. As I mentioned at my opening, I want to give you some color and some detail around the puts and takes of the quarter because I know there was a lot out there. And I think it's important to be able to link back to our guidance.

So we had guided adjusted EPS of $0.90 to $0.92. If you take the high end of our guidance, here's the puts and takes that you should consider. We had $0.02 of pressure from the SFC acquisition. That was $0.03 of fair value inventory step-up, offset by $0.01 of goodness from operations. We had $0.03 of pressure from the additional tax expenses I mentioned from a higher tax rate. We had $0.02 of favorability from FX, and we had a $0.03 – overall, we had a $0.03 operational beat.

So a way to look at this from a clean perspective on the operating power of the business in the quarter is we had a $0.95 operating quarter, and we improved operating margins on an apples-for-apples basis. And so as you think about what we delivered for the quarter, that is the clean view of what we delivered for the quarter.

Okay. Let's turn now to the segment discussions. I'm on slide six, and let's start with Fluid & Metering. In the quarter, orders decreased 1%, and organic sales were flat. Operating margin increased 340 basis points. That was driven primarily by the fair value inventory step-up that we had last year when we bought Alfa, and that was a $2.5 million impact in the third quarter of last year. Our energy markets, I've already talked about generally in a little bit more detail.

Aviation remains good for us. Obviously, the low fuel price and what we're doing to develop channels is helping us improve that market, but certainly being offset by what we're seeing in the mobile markets and in LPG, which remains challenged.

Water has been a good story for us. The municipal markets remain solid, especially around water services.

Industrial, I've talked about quite a bit already. We are seeing sequential stability. Day rates are holding. I think that the biggest thing that we're seeing that is a negative is we've seen projects – not big projects because, as you know, we typically are not involved in big projects. But whether it's an FMT or the industrial aspects of HST, we have seen projects pushed out and delayed and/or cancelled. And that is putting some pressure on the forward-looking point of view in terms of sales in the fourth quarter of this year.

Ag, as I said, that still remains soft, but we have seen some positive movement here in the fourth quarter. Again, while we like the sustained improvement, we're certainly not ready to call it a significant turn. And so I think we're going to see a little bit better results than we've seen here in the past, but – and we've hit a bottom, but I do think it's too early to call for a major upturn.

With that, let's turn to slide seven, and we'll talk about Health & Science. As I mentioned before, the life sciences and the scientific markets remain positive. These are businesses that have been on a nice growth trajectory here for quite some time, and we're excited about where we sit in the marketplace. That has been offset by the industrial-facing portions of that segment.

So about half of the HST is traditionally scientific and life science-related, and about half has an industrial aspect to it. And so we're seeing the offsets of the strength and the weakness in those markets.

We did see 4% organic order growth in HST in the quarter. We did have organic sales that were down 1%. Operating margin decreased 140 basis points really from everything I've talked about with the fair value inventory step up with SFC.

In Scientific Fluidics, again continues to be strong. The major end markets are doing well and exceeding expectations. The three markets of analytical instrumentation, bio and IVD have all delivered at or above our expectations, and we expect that to remain throughout this year and continue to have a good story into next year.

Sealing solutions, the scientific part of that is going into semiconductor is doing well. The part in oil and gas, obviously, has been challenged. And we love what SFC brings to this part of our business.

Industrial side, I already mentioned the weakness that's been there. We did see some weakness specifically around our industrial-facing businesses and HST, our gas, our micropump business and the industrial parts of material process. And so, we are keeping a close eye on those things going forward.

And then finally, in MPT, our material process business, the pharma story continues to be good but the longer cycle CapEx has seen some pressure as I mentioned before.

All right. I'm on our final segment. I'm on slide eight, and that's Diversified. Organic orders increased 4% in the quarter but it was down 6% in organic sales. Margins were down 750 basis points. They're exactly what we expected to happen. You had the impact of the step up from AWG, and you also had the mix impact that we would expect from new businesses coming in that have more amortization and bring down the overall portfolio mix.

Going forward, we think an op margin in the 25% range is where we'll sit today, but you should expect us to improve that over time as we bring AWG and Akron, those margins forward. We've talked about a 500-basis-point improvement over time. And there's no reason to believe that that won't happen. Our integration is going – on both of those are just going well and we're happy with the progress.

In terms of dispensing, it's been a fantastic story. The business continues to outperform. X-Smart has been a huge winner for us in this business. We are executing well in all three major regions, and we expect that to be a good new story going forward.

In fire and rescue, obviously the big news is bringing Akron and AWG into that portfolio, driving the synergies in the business. We are seeing some nice improvements already. Our integration is going well. We did hear in early in the fourth quarter announced internally that we are doing some restructuring around a facility consolidation and driving the benefits of this business. So you will see a restructuring charge in the fourth quarter, and we're doing exactly what we said we'd do.

In terms of BAND-IT, we're seeing strength in transportation in that business offset by weakness in oil and gas. So really the same headwinds we've seen in the past. But they have just done, once again, a terrific job on profit execution, focusing on niche markets where they can go get some growth and we really like this business for the long-term.

All right. I'm on our final slide, I'm on slide nine and I want to talk about the fourth quarter and full-year guidance. So in the fourth quarter, we estimate EPS to be in the range of $0.92 to $0.94. That allows us to maintain at the midpoint of our guidance, and for the year $3.72 to $3.74 despite the headwinds that we've talked about. So, there has been a little bit of confusion about, again, the underlying operating earnings, so let me walk you through that a little bit.

So we're guiding $0.92 to $0.94 of adjusted EPS. That's going to include about $0.02 of pressure from the SFC acquisition. So that's – when we think about that, you're going to have some incremental step up, right, and then you're going to have the operating impact. So we're going to get about $0.03 of operating goodness from SFC in the quarter, but it's going to be offset by $0.05 of inventory step up. So it's going to be $0.02 negative. And we're going to get another approximately $0.01 a pressure from the divestiture. So, again, while we're guiding $0.92 to $0.94, the underlying operating capability is more like $0.95 to $0.97. And you can see how that impacts the quarter and again, what that looks like for real operating capability for the year.

A few more modeling items. We expect organic revenue growth of approximately 1% in the quarter. Operating margins will be 19.5%, but again, that includes the $5.2 million of step-up. So we're going to have a nice strong operating profit margin on an ongoing basis as we think about the fourth quarter and exit rate into the year. You should expect the tax rate to be back to its 27% rate, so not at the 29.6% that you saw this quarter.

All right. For the full year, we expect organic revenue to be down 1% and adjusted operating margin to come in at about 20.5%. So, really outstanding profit margin given all the things that we've discussed. We expect full-year CapEx to come in at $40 million, free cash flow to be about 120% of net income. And in total, we'll reduce our share count by about 1% for the year given we've already executed in the year.

As always, as we think about our guidance, we don't include anything from future acquisitions or divestitures, any charges related to pension settlements or any cost related to restructuring actions.

So with that, let me turn it over to the operator, and we'll it open it up for questions. Thank you.

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Our first question comes from the line of Allison Poliniak with Wells Fargo Advisors. Please proceed with your question.

Allison A. Poliniak-Cusic
Analyst, Wells Fargo Securities LLC

Q

Hi, guys. Good morning.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Hi, Allison.

Allison A. Poliniak-Cusic
Analyst, Wells Fargo Securities LLC

Q

Andy, could you delve into the sort of Health & Science a little bit more? I would say, I guess one of your customers was talking about concerns of oversupply, and obviously potentially NIH funding slowing, I mean, but obviously orders were strong. So, I'm just trying to reconcile the differences in those comments.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Yeah. So, I want to be careful here. We never talk about any specific customer, right?

Allison A. Poliniak-Cusic
Analyst, Wells Fargo Securities LLC

Q

Sure.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

So, I think, generally, if you step back and you look at that landscape, so whether it's, you're looking at genetic sequencing, analytical instrumentation generally, in vitro diagnostics more broadly, we're seeing the trends continuing to be very good. And you see, if you look at sequencing in particular, that's still going to be a double-digit growth market. It's a market that's going through changes. It's moving from, call it, a research tool to a production tool or a commercial tool. And so, you'll see changes in the landscape there. But we are positioned exceptionally well across that customer base in that market. And of course, our traditional markets in IVD and analytical instrumentation, what you can see across the board is strength. And if you look at funding that's expected assuming that the funding trends that we've seen happened, that's actually a pretty good new story. So, when it's all said and done, as I look at those markets over the next certainly a year and more into the future, I think that's a very good new story for us.

Allison A. Poliniak-Cusic
Analyst, Wells Fargo Securities LLC

Q

That's great. Thanks. And then obviously, you guys have done very well on the capital deployment side, deployed a lot towards acquisition this year. Just what's the prolonged sort of industrial malaise that we've experienced, I mean have you noticed any sort of changes in the M&A environment where there are people, especially in smaller business, they're trying to – are becoming more active in terms of setting themselves up for sale, pricing declines or anything in that nature?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

I don't think there's been a meaningful break yet in that. Meaning that some of the more expensive assets, are we seeing a more reasonable perspective on valuation, I wouldn't say that yet. When you look at the things that are in the energy markets, a lot of people, they had outside the expectations sometime ago. And now they're struggling with the reality of their operating capabilities, and so they're not ready to part with those businesses, it depress multiples. But our pipeline looks like it's booked for a long time, right? So, it's highly a cultivated pipeline. We've been working on it actively. And so that really doesn't change quarter-to-quarter very much for us.

What changes is the activity from the really the auction world. And what I would say is that from the auction world, that has slowed down here recently, the last two quarters, but that's not the principal piece of kind of how we think about M&A anyway. But I do expect there to be more activity going forward in our marketplace as people rectify what their operating capabilities really are in prices. So, we'll keep working at the way we've done it and try to drive it at the same kind of level that you would expect us to.

Allison A. Poliniak-Cusic
Analyst, Wells Fargo Securities LLC

Q

Great. Thanks so much.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Thanks, Allison.

Operator: Thank you. Our next question comes from the line of Steven Winoker with Bernstein. Please proceed with your question.

Steven Eric Winoker
Analyst, Sanford C. Bernstein & Co. LLC

Q

Thanks. And good morning, Andy and Mike.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Good morning.

Michael J. Yates
Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

A

Good morning.

Steven Eric Winoker
Analyst, Sanford C. Bernstein & Co. LLC

Q

Just a couple or a few quick questions. First, the exit rate for Q4 when you're thinking about that looking forward, you're talking about 1%. We had talked last quarter about sort of the reasonableness of the expectations at the time that you might hit a 4% organic growth in the quarter. And the early read, if you think about it, I guess, we talked about rescue tools, X-Smart, oil and gas, distribution, maybe just give us a better sense for your Q4 read now, kind of what are the biggest drivers of that change.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

You mean, looking at kind of a 3% or 4% up versus a 1% up, is that what you mean, Steve?

Steven Eric Winoker
Analyst, Sanford C. Bernstein & Co. LLC

Q

Yeah. Yeah. Yeah. Exactly.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Yeah. The biggest thing in there is really the day rates are actually – are very much what we've looked at, there're not a lot of change in there. But when you think of things that have a bigger CapEx component to it, you're seeing those things get pushed out. And those aren't big piece of our overall business, but they are – if you look at the marketplace and doesn't really matter what segment you look in, they're absent right now. And so, what I view is happening is this kind of continued pause and hesitancy around anything with a larger ticket item associated with it, that's the biggest change. But if you look at kind of general day rates that looks like it's looked like for a long time.

Steven Eric Winoker
Analyst, Sanford C. Bernstein & Co. LLC

Q

Okay. Okay. And then if I sort of extend that, I'm not asking for you guys to do this yet, but if I take the 1% for the quarter and sort of talk about 1% to 2% organic next year, you guys usually talk about like a 30% to 35% incremental on 3% growth. So if I take 25% to 30% here, that would normally give me like another $0.09 or $0.10 on the midpoint, plus almost the full $0.25 that you mentioned, because there'll be some overlap as that goes organic, that still get me kind of 8% to 10% EPS growth next year. Am I missing any kind of big movers in either direction there?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

No. I do think, right, the – when we come out with our guidance for the quarter, the pivot is going to be what do you think the underlying industrial growth rates are going to be, right? So your logic – I understand your logic. It's not dissimilar to how we're thinking about it. I'm not prepared to make that call here today, but your logic is sound.

Steven Eric Winoker
Analyst, Sanford C. Bernstein & Co. LLC

Q

Okay. And then one last just technical question, maybe more for Mike, I guess. Just help me understand why you didn't just borrow the money given interest rates today instead of repatriating back with the tax penalty and your low leverage levels?

Michael J. Yates
Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

A

Sure. Well, we went ahead and made a decision to bring the money back from all over the globe really to get the benefit today and optimize our balance sheet, and to get it out of some of the areas in the world where we did bring about $50 million out of China, actually. So we wanted to get that money out of China, and it made a lot of sense to us. And that was the real driver in some of the costs that we incurred in the quarter.

Steven Eric Winoker Q
Analyst, Sanford C. Bernstein & Co. LLC

Okay. That makes more sense. Thank you. I'll pass it on.

Andrew K. Silvernail A
Chairman and Chief Executive Officer, IDEX Corp.

You bet. Thank you.

Operator: Thank you. Our next question comes from the line of Scott Graham from BMO Capital Markets. Please proceed with your question.

R. Scott Graham Q
Analyst, BMO Capital Markets (United States)

Hey. Good morning, Andy. Good morning, Mike. Very nice quarter.

Andrew K. Silvernail A
Chairman and Chief Executive Officer, IDEX Corp.

Hey, Scott. Thank you.

Michael J. Yates A
Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

Good morning, Scott.

R. Scott Graham Q
Analyst, BMO Capital Markets (United States)

Hey. So, I just want to maybe ask a previous question little bit differently around organic growth, maybe kind of getting to the exit rate is the endgame. But more importantly for the full quarter, if you're expecting organic up about 1% in the fourth quarter and we were kind of down 2% this quarter, could you maybe tell us the segments where you see that delta coming from?

Andrew K. Silvernail A
Chairman and Chief Executive Officer, IDEX Corp.

So there actually isn't lot of puts and takes. You got some pretty consistent performance. We're not seeing kind of one thing driving major differences. That being said, if you kind of look at how it's flown, we've got about 2% incremental order growth in the quarter. And so I think we're in pretty good position relative to delivering on the quarter, but it'll be driven by kind of the day rate business. Mike, anything you'd add?

Michael J. Yates A
Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

No. I think FSD is a little stronger in Q4, that there're some strength there in the forecast, so that's part of it.

R. Scott Graham
Analyst, BMO Capital Markets (United States)

Q

Let me maybe – if I could just paraphrase this sort of the better markets are kind of staying better...

Michael J. Yates
Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

A

That's right.

R. Scott Graham
Analyst, BMO Capital Markets (United States)

Q

...and the weaker markets are getting less weak.

Michael J. Yates
Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

A

Well, I wouldn't say they're getting less weak. I would just say they're stable. Now, they're getting less weak on – as you start to look at year-over-year comparisons, right?

R. Scott Graham
Analyst, BMO Capital Markets (United States)

Q

Yeah. That's what I mean. Yeah.

Michael J. Yates
Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

A

Yeah. But from a sequential standpoint, things are looking like they've looked like for quite some time.

R. Scott Graham
Analyst, BMO Capital Markets (United States)

Q

I'm with you. My second question is maybe something I hope to get back to I think something we haven't talked about in a while and your driving of the margin continues to impress. I guess in the past, you guys used to talk about a certain dollar level of productivity savings, and I know you think about that a little bit differently now, Andy, but for the sake of modeling, one of the things that I talked about with Heath from time to time was something north of $30 million, south of $40 million of productivity has been kind of the last couple year goal. Is that still in the realm?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Well, I think how we've talked about it for a long time here now, Scott, right, is you start the year with kind of, we'll call it, natural inflation. And today, given the kind of material prices, that's just not a big number right now. But you go end of the year with just wage inflation and basic overhead inflation that looks like kind of $15 million or so, it could be $15 million to $20 million, right. So to hold your own, you got to cover that. That's the starting bogey.

And then to drive incremental profitability and margin expansion, that's where you start to have to get kind of north of $20 million. And that's been our consistent goal historically is be able to drive productivity. So we're getting net benefit. And so, that's why we've always talked about our ability to drive incremental margins even in a low growth environment. So even if you have a low-single-digit organic growth environment and you think about our ability to continue to get price, we would expect to see margin expansion.

R. Scott Graham
Analyst, BMO Capital Markets (United States)

Q

Yeah.

Michael J. Yates
Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

A

And that allows price then, Scott, to kind of flow through if we can get productivity to kind of offset inflation and material inflation.

R. Scott Graham
Analyst, BMO Capital Markets (United States)

Q

Yes. No, I get it. My number was a gross number. So I think we're on the same page. Thanks a lot.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

No problem at all, Scott. Thank you.

Operator: Thank you. Our next question comes from the line of Nathan Jones with Stifel. Please proceed with your question.

Nathan Jones
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Good morning, guys.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Hi, Nathan.

Michael J. Yates
Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

A

Good morning.

Nathan Jones
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Andy, I wonder if we could try and [ph] parse (34:46) out a little bit more into the industrial end-markets. And where you've seen – maybe things be better or less bad and where you've seen things be maybe a little bit worse. I know it's kind of hard [ph] thing (34:59) and a lot of it goes through distribution. But just any color you could provide there?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

One of the surprising things in this marketplace is once we've got passed kind of the steep drop in the energy related markets, right. Then what you saw happen was this ripple effect that went across the general industrial landscape. And so it is a little bit of an unusual situation right now where you're seeing performance across the industrial landscape, all look pretty similar.

So if you were to look at say, our gas business, our Viking business, Warren Rupp, BAND-IT things that are kind of, that sits centrally and I'm going to call it general industrial. It is surprising how evenly split across to the different markets, the malaises. And so again, we had to get past that kind of commodity-driven issues, but I think one of the signals that that sends to me Nathan, is again kind of back to this – I want to call this, it's a big pause that's been out there for quite some time. And people are looking for a catalyst.

And so we see it up and down the supply chain, we see it from our customers back through how we're behaving in our supply chain. And everybody is at that pause, so you see it from how capital's being deployed meaning big CapEx to the interval of orders. So where in the past, you'd see larger blanket orders in annual time frames, in quarterly. A lot of that stuff has just gone away. You're now dealing in a world of general releases.

And so, again, it's surprising how general this is. Obviously, I think the energy markets are still worse than kind of anything with some – volatility depends upon the price of oil. But across the rest of the industrial landscape, it's surprisingly cohesive what we're seeing.

Nathan Jones
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Surprisingly cohesive in a non-cohesive market?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

That's exactly right Nathan.

Nathan Jones
Analyst, Stifel, Nicolaus & Co., Inc.

Q

So, I guess maybe a little philosophical question for you here that maybe talk a little bit about 2017. We've seen a lack of volatility in oil price over the last, probably six months.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Yeah.

Nathan Jones
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Prices are high, things are better. Is that something that you would expect to play through as that kind of general ripple effect across general industrial market in a more positive way if we can maintain that kind of at least stable and maybe improving energy prices?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

So the short answer to it is yes. I think that the magnitude is what you have to put your finger on. So if you see oil prices back in this $50 to $60 range, it's going to be a slow roll of how that impacts things over time, right? So you'll get the impact of production happening. You'll get the wellhead impact. But how that may moves its way through the general economy, I think, will take some time.

Nathan Jones
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Fair enough. But could you just give any more color on the different parts of the water markets that you're playing in? There's been a few reports just went out this morning from a water player that – with not such great results, just what you're seeing there.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

The water services is where the strength is right now. If you kind of look at that, for us – so our – so as an example, our ADS business has had terrific results. Some of that, I think is taking share. Some of that has been a decent spend in the municipal space.

I think – I've said in the past that I thought municipal was going to have some good legs here for the foreseeable future. I still believe that to be true, but let's make sure that we're watching that quarter-to-quarter, and what happens there. But for us, water services has been the brightest spot.

Nathan Jones
Analyst, Stifel, Nicolaus & Co., Inc.

Q

All right. Thanks very much.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Thanks, Nathan.

Operator: Thank you. Our next question comes from the line of Brett Linzey with Vertical Research Partners. Please proceed with your question.

Brett Logan Linzey
Analyst, Vertical Research Partners LLC

Q

Hi. Good morning, guys.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Hey, Brett.

Michael J. Yates
Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

A

Good morning.

Brett Logan Linzey
Analyst, Vertical Research Partners LLC

Q

A great quarter. Hey. Just wanted to circle back on the completed deals for this year.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Yeah.

Brett Logan Linzey
Analyst, Vertical Research Partners LLC

Q

Clearly strong free cash flow generation in the quarter. Do those deals come into the next neutral to free cash flow conversion? Just trying to get a sense as to what the opportunity is outside margins and growth...

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Okay.

Brett Logan Linzey
Analyst, Vertical Research Partners LLC

Q

...but more focused on free cash flow and the 120% conversion you're doing this year and expectations going forward.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Yeah. So I think I'll let Mike comment on it this also. So generally, right, these are going to be accretive to free cash flow conversion because of the amortization effect, right? So...

Brett Logan Linzey
Analyst, Vertical Research Partners LLC

Q

Yeah.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

...you're going to see that positively generally. And they're all asset-light businesses. None of these businesses that we brought on are heavy capital in any way. And so you'd expect to see across them really improvements in working capital over time, improvements in margin. No need to inject big CapEx, so they should be positive. Is that fair, Mike?

Michael J. Yates
Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

A

Yes, that's right. All three deals helped cash flow in the quarter, right, because they may not help earnings because of the step-up in the amortization, but on a cash basis, definitely helped the free cash flow in the quarter.

Brett Logan Linzey
Analyst, Vertical Research Partners LLC

Q

Okay. No, that helps. And I guess shifting gears to FMT, obviously very good margins there. Are you able to order-rank the contributors of that margin expansion between net restructuring carryover, mix, leverage? I mean, it just seems like a very big number, just trying to understand the kind of parts of different pieces there.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Yes. Yes. Three things kind of happening there, right? The first one is some of our bigger businesses within there, they did restructuring last year, right, and we're certainly seeing the benefits of that. Second is you've got some positive mix, but that's not a big number.

But third and importantly, we've talked a lot about the impact of our fixed businesses, and we've had great results from that and a bunch of those businesses sit in the FMT portfolio. And I really should say, I should add price, right? We continue to get positive price in FMT and those are, really it's four things not three that really matter and continue to drive our margin expansion.

Brett Logan Linzey
Analyst, Vertical Research Partners LLC

Q

Okay. Great. I'll pass along. Thanks, guys.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Thanks, Brett.

Operator: Thank you. Our next question comes from the line of Deane Dray with RBC Capital Markets. Please proceed with your question.

Deane Dray
Analyst, RBC Capital Markets LLC

Q

Thank you. Good morning, everyone.

Michael J. Yates
Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

A

Hey, Deane.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Hey, Deane.

Deane Dray
Analyst, RBC Capital Markets LLC

Q

I was hoping to stay in Fluid & Metering for a moment. And Andy, if you could expand on the point about some of the push outs you saw in the quarter...

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Yeah.

Deane Dray
Analyst, RBC Capital Markets LLC

Q

And maybe this is all part of that general pause and some hesitancy on bigger ticket items. But some context there, these pushed into 4Q or is it uncertain when they would actually come through?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

I think it's uncertain, Dean. I think we've talked about this in a number of the past quarters that we see things get kind of pushed, delayed, whatever. And my view is that until you get some confidence back in, these things are going sit out there, so anything we've kind of big ticket CapEx associated with them. And so, if you look at energy as an example, you're going to see – if you assume that energy prices kind of are in that $50 or $60 range, you'll see excess capacity get absorbed in 2017 and then you'll see new CapEx coming in at 2018. And while that tends to be more cyclical than the rest of the general industry, I think it's a good proxy for what we're seeing across the industrial landscape.

Deane Dray
Analyst, RBC Capital Markets LLC

Q

Okay. That's real helpful. I mean, just to make sure we've got the modeling set up for the fourth quarter, you've mentioned a couple different charges. So there's restructuring and Fire & Safety, and there's also going to be a pension charge?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

That's right.

Michael J. Yates
Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

A

Yeah

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Yeah, that's right. So we haven't put our arms around exactly what those will look like. But obviously, we'll provide the details. So we'll do some restructuring as we expected we would when we did those acquisitions and the pension will play itself out here in the fourth quarter.

Deane Dray
Analyst, RBC Capital Markets LLC

Q

And that's a mix of cash and non-cash?

Michael J. Yates
Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

A

That's all cash. The pension will be cash, about 75% of it will be cash and then the restructuring will be mostly cash also.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Yeah. Yeah.

Deane Dray
Analyst, RBC Capital Markets LLC

Q

Got it. And then just last question, any update on the CFO search, any timing expectations?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Yeah, our general expectation is these things kind of take six months or so. And so if you focus in around the end of January, some time into February that would be our expectation for finalizing it.

Deane Dray
Analyst, RBC Capital Markets LLC

Q

Great. Thank you.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Thank you, Deane.

Operator: Thank you. Our next question comes from the line of Matthew Mishan with KeyBanc Capital Markets. Please proceed with your questions.

Matthew Mishan
Analyst, KeyBanc Capital Markets, Inc.

Q

Thank you. Good morning, Andy and Mike.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Good morning.

Michael J. Yates
Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

A

Hi, Matt.

Matthew Mishan
Analyst, KeyBanc Capital Markets, Inc.

Q

Hey, I wanted to drill down a little bit further into the life sciences. The orders were clearly very strong there in the quarter. But the customer that warrant, they didn't really see it until like late in 3Q and then really took down 4Q expectations. Couldn't that result in a bit of an inventory overhang for you? And then can you also talk a little bit about what you're seeing with some of your broader life science customers later in the quarter and early in the fourth quarter? And should we feel confident that it's a general mix or a single customer, let's call it the transitory headwind and not a little bit broader?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Yeah. So again, I want to be really, really careful. We don't comment on any specific customer. So we are where we sit in the food chain, right. What we experience in our numbers tends to be – it's already played out for us by the time it's played out in the markets for our customers generally, right, just because of how that works in the supply chain and timing, et cetera, right?

And so we don't see a major change in the fourth quarter based on anything you see out there in the marketplace. And also I think it's really important to note that this is – we're talking about no customer being more than 2% of sales, right? So we don't have a single customer that is material to the IDEX results as we think about that in the portfolio.

So with that said, as I think about the broader life sciences market, I think there is always bumps in there. Every six or so quarters, you'll see a bump in these marketplaces based on when products are shipping, et cetera, product life cycles, supply chain, but the story is a good news story. We've seen strength in those markets. We expect to see strength in those markets going forward, and for those to be above the IDEX average in terms of growth.

Matthew Mishan
Analyst, KeyBanc Capital Markets, Inc.

Q

Okay. Great. And just a bigger picture question for me on the type of – on the projects that are being pulled. What do you think needs to happen for those to be given the thumbs up from your customers?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

I think it's a combination of sustained improvement in a commodities world. And this sounds like such a weak answer, but confidence. There is a general lack of confidence in spending money and putting yourself out forward and putting a lot of capital forward. And so I think that confidence is a combination of two years of a pretty soft market, a very uncertain political environment that people just aren't comfortable with how things are going to play out, and I think that really needs to happen.

A little bit of improvement in the overall economic growth rate would go a long way. Certainly, people are seeing this starting to play through in wage inflation if you see what's kind of happening in the global marketplace. So you're seeing some elements of it spark there. But in general, you're not seeing that catalyst that's going to push that forward. And as we think about our 2017 planning, we don't see a catalyst, right? We don't see that happening. We're well-positioned to deal with it if it does. We've always said time and again that we are very able to react on the upside and we never want to get caught on the downside.

And so from our ability to mobilize and execute in a faster environment, we feel really comfortable around that in terms of the supply chain and our ability to produce. And at the same time, we think that this environment is going to continue here into 2017.

Matthew Mishan
Analyst, KeyBanc Capital Markets, Inc.

Q

Right. Thank you very much.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Thank you.

Operator: Thank you. Our next question comes from the line of Walter Liptak with Seaport Global. Please proceed with your question.

Walter Scott Liptak
Analyst, Seaport Global Securities LLC

Q

Hi. Thanks. Good morning, guys.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Hey, Walt.

Walter Scott Liptak
Analyst, Seaport Global Securities LLC

Q

Hey, I wanted to ask about the productivity gains that you're getting, and I'm wondering what inning you are in kind of the process that you've been doing to get margins that were there now.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Walt, I feel really comfortable that we can continue to drive productivity. I'd say what's accelerated our gains this year has been around the focus we've had on about one-quarter of our portfolio that are fixed businesses. We told you earlier in the year that that makes up about 25% of our business. Into this year, we are almost 300 basis points better in profitability around those businesses. And so that's been a very, very good news story.

And must keep in mind, too, that we're delivering this kind of margin profile with some of our bellwether and most profitable companies struggling, right? That have really been hit most by this commodity and overall industrial distribution. So if you think about Viking, Warren Rupp, BAND-IT, Banjo, and even Rescue Tools, right, so Rescue Tools, it's a different struggle for Rescue Tools because of the weakness in emerging markets around sovereign budgets.

But if you look at those five businesses, those are big profit contributors to this company, and they have been hit squarely with the headwind. And what we've been able to do is being able to really deliver quality of earnings in those businesses, continue – it's very, very high quality of earnings in those businesses and cash flow, and at the same time still drive overall margin potential with what we're doing in the rest of the business. And so when I think about our execution and our positioning for any kind of improvement, we're in a good spot.

Walter Scott Liptak
Analyst, Seaport Global Securities LLC

Q

Okay. All right. That sounds great. Is there a number that we can think of? I mean, I know you give the leverage number, but in terms of where you think you can get adjusted operating margins as you go a couple of years out, is there like a number that you think the whole business can get to?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

You know what, with modest growth, with modest growth, a couple of points, right? We can get 50 basis points plus.

Michael J. Yates
Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

A

Yeah. I think 50 basis points to 80 basis points of margin improvement, Walt, is what we've kind of said.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Yeah with a couple of points of growth and that breakeven point, when I say breakeven point, I mean the point at which we can still expand margins has gone down substantially, right? And our ability to drive productivity. And so if we continue to see a soft environment, we'll still get better margins going forward.

Walter Scott Liptak
Analyst, Seaport Global Securities LLC

Q

Okay. That's great. All right. Thanks guys.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Thanks, Walt.

Operator: Thank you. Our next question comes from the line of Jim Foung with Gabelli & Company. Please proceed with your question.

James V. Foung
Analyst, Gabelli & Company

Q

Hi. Good morning, Andy.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Hey, Jim.

James V. Foung
Analyst, Gabelli & Company

Q

Good quarter and core earnings here.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Thank you.

James V. Foung
Analyst, Gabelli & Company

Q

So I'm going to ask you, so pro forma for the year recent acquisitions, how much of your businesses are now moving to book and ship versus capital projects?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

The vast majority of our businesses are, we're looking at book and ship, right?

James V. Foung
Analyst, Gabelli & Company

Q

Right.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

I'm not sure I can give you a specific number. But big capital projects, they've never been a big piece of our business, but they can swing. They can certainly swing in terms of volatility in any one quarter. And some of that we're seeing right now. But historically, we go into a quarter with half the quarter booked. And you've got to deliver a book and ship in the quarter of about half the business. And so that's what that kind of looks like now for us no material difference. The difference is I think that the larger CapEx related thing that we have had in the past and were a buffer, those have certainly been pushed or cancelled.

James V. Foung
Analyst, Gabelli & Company

Q

Right. So at the margin, that can be a swing for you [indiscernible] (53:01)

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

It can. And if you look at kind of where we stand today on our expectations for fourth quarter organic, that's the big pivot. But at the same time, we're finding ways to cover it, right? We're finding ways to still grow income and do a great job around cash.

James V. Foung
Analyst, Gabelli & Company

Q

Right. Okay. And then could you just talk about that 500-basis-point improvements from the acquisition of AWG and Akron? And I think it's also – with maybe SFC, what kind of positive surprises you might see there.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Well, I think – let me talk about SFC first. That's a very high-margin business, and that is really around our growth story.

James V. Foung
Analyst, Gabelli & Company

Q

Okay.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

So that's our focus with SFC. And by the way with AWG and Akron, growth is a critical component to the overall story. But recognizing that when we bought the businesses we saw more opportunity to get the margin profiles in line with our core IDEX business, and that's about 500 basis points in total. And Akron has been part of the portfolio a little bit longer. Earlier in the year, we bought the business. We had great results so far with it. And AWG is a terrific fit, and you can put that together with our other safety and rescue assets, there is a lot of opportunity to grow the business and to improve margin profile.

James V. Foung
Analyst, Gabelli & Company

Q

Any kind of timetable in terms of when you might see the margin improvement coming?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

I think what we've said in the past, and I wouldn't change it, is there is no reason you wouldn't see a couple of hundred basis points kind of out of the gate with those businesses, and then the balance over kind of three years. So...

James V. Foung
Analyst, Gabelli & Company

Q

Right.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

I think it takes three years to get 500 basis points. But there is no reason you wouldn't see a couple of hundred basis points in that first year.

James V. Foung
Analyst, Gabelli & Company

Q

Great. Thank you so much. That's all I have.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Thank you, Jim.

Operator: Thank you. Our next question comes from the line of Jim Giannakouros with Oppenheimer. Please proceed with your question.

Jim Giannakouros
Analyst, Oppenheimer & Co., Inc. (Broker)

Q

Good morning, Andy, Mike. Thanks for taking my question.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

You bet, Jim.

Jim Giannakouros
Analyst, Oppenheimer & Co., Inc. (Broker)

Q

So your comments on 4Q restructuring, were they isolated to integrating your recent acquisitions or are there other restructuring actions potential in play just noting that historically you've taken the opportunity to do some of that activity in other segments?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Yeah, Jim. So the bulk of it is from the acquisitions but there are few other areas that we're taking the opportunity to do some consolidation and get some leverage. And so we'll see some improvements in some other businesses also.

Jim Giannakouros
Analyst, Oppenheimer & Co., Inc. (Broker)

Q

Okay. And then to understand the divestures, I know that they're small, but was there a certain growth profile that just didn't make your – you didn't see the outlook as strong as you would like or certain margin profile that just didn't make the cut? What drove the decision to divest each of those and did you mention – and I missed it if you did, what that third divesture was in early October?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Yeah. So let me talk about kind of the rationale behind it. So when we think these things, it's not necessarily just a growth profile that we're looking at. It's really around how are they going to be advantaged or disadvantaged long-term with us as the owners, right? And so with the things that we have sold, we have sold them principally to people who have one of two things, either a different expectation of long-term performance than we have, but more importantly, the ability to better position that business with an asset that they own. And we have elected to not make the investment to get that competitive scale.

So what you're seeing us do [ph] are (56:52) sell relatively small things or very small things that don't have a unique advantage today that really need some kind of relative competitive scale. And we are selling those things that we don't – we have decided that it's not worth the organic or the inorganic investment to us if the opportunities are elsewhere, and that's really how we've been making those decisions.

And also keep in mind, things that are small and don't have the kind of advantage that we look for in a business, they take a lot of management time, right? They are disproportionate in what they require from a management time and we'd rather put those resources elsewhere.

In terms of – have we said about the businesses, the third business? Mike?

Michael J. Yates
Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

A

No.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

We have not published that yet, so we won't do so. But we're talking something that's small. You'll see it as things roll out here in the next few weeks.

Jim Giannakouros
Analyst, Oppenheimer & Co., Inc. (Broker)

Q

Got it. Okay. And one last one, if I may, and I apologize if I did miss it. When you talk about FMT, you talk about general industrials kind of being the swing factor there as far as your organic prospects. But did you comment specifically on CFP? And if not, could you get a little granular there on what you're seeing in those specific end-markets?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Yeah. So you're really talking about Viking and Warren Rupp for the most part. When you say CFP, that's the bulk of it, right, Richter and whatnot. It's really the same factors we're talking about generally. Those are the big pieces of our FMT business that's based in the general industrial world. And they've had a tough go in 2017, right? They've been hit disproportionately to the pressures that we're seeing in the energy and the general industrial markets. But again, all of those businesses have seen kind of sequential stability in their day rate business with some incremental negative on the CapEx side.

Jim Giannakouros
Analyst, Oppenheimer & Co., Inc. (Broker)

Q

Got it. Thank you.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Thanks, Jim.

Operator: Thank you. Our next question comes from the line of Charlie Brady with SunTrust Robinson Humphrey. Please proceed with your question.

Charles Brady
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Hey, thanks. Good morning, guys.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Good morning.

Charles Brady
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Just a quick one on the commentary on ag, saying that you saw a slight uptick. I know you're not calling the market, but, I mean, I can't recall anyone else saying ag is up, so...

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Yeah. That's why we want to be very careful in saying, I'm not going to call this an inflection point. I think that would be a mistake. We saw some improvement in the quarter, right? It's been a tough story overall. But we did see some sequential improvement in the quarter and some year-over-year improvement in the quarter. But I think let's be hesitant on that one. It was good to see, but we got to have a lot more data points before I'd make any commentary that I think it's – we've seen a sustainable inflection.

Charles Brady
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Yeah. Can you expand on what you think drove some of that strength, even if this is only temporary, kind of what was behind that?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Charlie, it's probably depleted inventories just in the channel and a pent-up demand for the replacement parts. It's been down for almost seven quarters.

Michael J. Yates
Interim CFO, Vice President and Chief Accounting Officer, IDEX Corp.

A

Yeah. I think it's more replacement parts than it is equipment pickup. There is still a lot of equipment in the channel. There's a lot of equipment in the field. There's a lot of equipment in the channel. So it's really a replacement part story versus a meaningful uptick in equipment.

Charles Brady
Analyst, SunTrust Robinson Humphrey, Inc.

Q

Got it. Thanks.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Yeah.

Operator: Thank you. [Operator Instructions] Our next question comes from the line of Joe Giordano with Cowen & Company. Please proceed with your question.

Joseph Giordano
Analyst, Cowen & Co. LLC

Q

Hey, guys. Thanks for taking my questions here.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Hey, Joe.

Joseph Giordano
Analyst, Cowen & Co. LLC

Q

In terms of orders of HST, and fully appreciating your comments about the [ph] materiality (01:00:58) of any specific customers, but that segment order has been down – flat to down for the last five quarters. So I was a little surprised that this would be the quarter that you start seeing it perk up here. Is that more of a function of comps just getting easier or you're seeing anything specific in that market that's kind of driving out here?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.
A

Yeah. I wouldn't say there is any major change. As you – and we did note that the back-half comp starts to get easier. So it's – hey, we're glad to see it. It's good to see. But there is no major inflection different from what we've talked about so far.

Joseph Giordano
Analyst, Cowen & Co. LLC
Q

Okay. And just related to like the commentary you've heard from the major players in that space, do you get a sense that maybe like a slowdown in financing and just deal activity in that healthcare space is just putting kind of a little bit of a crimp in just spending and capital spending there? Is that – do you think it's deal-related in a way?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.
A

I'm not sure I understand the question, Joe. Are you saying because of...

Joseph Giordano
Analyst, Cowen & Co. LLC
Q

So a lot of like the sequencing, it's still more on the research side, and the lack of just like funding in the market, so it's capital funding for small companies in that space. Do you think that's impacting just overall demand there a little bit like a more of a temporary thing in that sense, because I know you have this view – a long-term view is very positive there.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.
A

Yeah. I don't think so. I think you've got – when you're talking about sequencing, right, you've got major product cycles that are critically important, right? And you've got this movement from, I'll call it the lab space into more of a commercial application. And so that is a move that everyone has expected to happen.

And with that, you see a movement from very, very high-priced equipment down to more readily available lower-priced equipment that is more deployable into the field. I think – when you step back and think about the potential for this industry and you look at the number of sequencers that are sold per year compared to say the number of mass back or analytical instruments in ultra high pressure chromatography, it's tiny. I mean it's absolutely tiny. And when you look at the applications and where those can go and land and the number of potential units that can be sold into a commercial applications and when I say commercial I mean non kind of laboratory research...

Joseph Giordano
Analyst, Cowen & Co. LLC
Q

Sure.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

...the number is huge. It's multiples of what's sold today. And so, it's not going to be smooth, right? It's not going to be perfect. But if I think five years from now or 10 years from now compared to where we are today, and the unit volume that you would expect, it's going to be much, much, much higher and that's the bet we're making.

Joseph Giordano
Analyst, Cowen & Co. LLC

Q

Okay. That's fair. And then if I can get to sneak in one last one on the divestments. You mentioned that the stuff that you've been buying a little bit more asset light than maybe the average. Is there any consistent – in the divestments, is this kind of move to asset – further asset light the portfolio or are these kind of on a high-end in terms of average?

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

No. I wouldn't read into that at all. Across our business, we're pretty asset light. You're talking about 1.5%, 2% CapEx density for the businesses. We're not necessarily buying things that are lower than that or selling things that are higher than that. It's really around market positioning. Market positioning what I would call relative competitive scale, right? So if you look at what really works for us, it's when we are in a niche that's big enough to be attractive but small enough to not get the gorillas of the world if you wanted to compete for it. And then we have an attractive relative market share position. So we are kind of a classic number one or number two. And the profit pools in that scenario and the attractiveness is very, very high. When you are a distant three, four, five and you don't have a pathway or if the niche is too small, that's where it's just not very attractive for us.

Joseph Giordano
Analyst, Cowen & Co. LLC

Q

Makes sense. Thanks, guys.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

A

Thanks, Joe.

Operator: Thank you. Ladies and gentlemen, that concludes our question-and-answer session. I would like to turn the floor back to Mr. Silvernail for final remarks.

Andrew K. Silvernail
Chairman and Chief Executive Officer, IDEX Corp.

Well, thank you very much, and thank you everybody for joining us on the call today. I think as I open this up, my hope is that people will really focus in on what we've done to drive operating results and what we have the ability to do, kind of given this continued weak macro environment. And again, I think our overall execution has been extremely strong. The underlying operating earnings of this company, and our potential to drive earnings growth over time, I think is substantial. We've done a nice job with disciplined capital deployment, and we've got a great balance sheet to continue to do that.

So look, we're going to have to continue to work through this murky, macro environment that is going to be with us for a while. But we are exceptionally well positioned to drive total shareholder return as we go forward.

So again, thank you for your questions today, and thank you for your support for IDEX, and we'll talk to you here in about 90 days. Take care.

Operator: Thank you. This concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation.