First Quarter 2024
Earnings Conference Call
Prepared Remarks

May 3, 2024

Trimble Corporate Participants

Rob Painter – President and Chief Executive Officer
Phil Sawarynski – Incoming Chief Financial Officer

Rob Painter, CEO

Welcome, everyone. Before I get started, our presentation is available on our website, and we ask that you refer to the safe harbor at the back. Our financial commentary will reflect non-GAAP performance metrics including organic growth comparisons, which refer to the corresponding period of last year unless otherwise noted. In addition, our P&L commentary will primarily emphasize our as-adjusted numbers, which exclude our agriculture business, better reflecting Trimble on a go-forward basis.

Starting on slide 4, during the first quarter we continued to advance our Connect & Scale strategy, which involves digitally connecting the workflows within targeted industry segments and creating scale across Trimble through shared technology platforms. Our strategy delivers outcomes in the form of unique value to our customers and sustainable value creation to our shareholders. We want to convey three key messages today, starting with the solid performance in the quarter, where all three segments performed ahead of expectations, as detailed on slides 5 and 6. $2.03B of ARR grew 13% organically, as-adjusted revenue grew 8% organically, as-adjusted gross margins were a record 67.5%, as-adjusted EBITDA margin expanded 290 basis points to 27.9% and free cash flow was strong at $227M. We are confirming our previous total year guidance, despite unfavorable currency moves, and we will provide an update in our next call as we build confidence in the months ahead.

Key message number two is a strategic portfolio highlight. In the first quarter, we divested certain water monitoring assets, our 21st divestiture in the last 4 years, and on April 1 we closed our PTx Trimble joint venture. I'm proud to have established this precision agriculture joint venture with Eric Hansotia and his team at AGCO. This is a high character team with a bold vision. These moves simplify and focus our organization and provide cash to strengthen our balance sheet and support our capital allocation strategy.

Key message number three on slide 7 is that our new reporting segments are in place, which align to our new organizational structure. We provided historical data on the segments to our investors on April 12th. It takes an enormous amount of work to affect change on this scale and I'm grateful to our Trimble colleagues for their courage and dedication. The sum of these actions will simplify and focus our business, thereby enabling us to reset to a new and better baseline as we aim to perform to our full potential. As evidence, on an as-reported basis, our first quarter revenue was 73% software, services and recurring, and 58% recurring, while on an as-adjusted basis, our first quarter revenue was 77% software, services and recurring, and 63% recurring.

Turning to the segments, let's start on slide 8 with our AECO segment. Connect & Scale is well in motion here, and it is working. Connect is about connecting users, data, stakeholders and workflow across the industry life cycle continuum. Our right to win starts with the breadth, depth and connectedness of our offerings. It bookends by delivering solutions that connect the physical and digital worlds. Scale is about making Trimble easier to do business with and enabling efficient and effective growth. In the quarter, we moved our go to market team to an account based selling model, we expanded our pre-packaged Trimble Construction One offerings, and we released our next version of systems transformation which is providing us new insights into our customers. Mark Schwartz and his team delivered record first quarter bookings, an 18% increase in ARR and margin expansion of 430 basis points. This business is a multi-year overnight success, and we trust the new reporting structure now gives enhanced visibility to the quality of the business we have been transforming over the last few years. To emphasize the point, this is a scaled $1.1B ARR segment operating as a rule of 40+ business. In fact, a rule of 50+ in the quarter. Market conditions remain favorable at the moment, with strength in sub-segments such as reshoring and onshoring of manufacturing, EV and battery plants, data centers, and renewable energy projects.

The physical side of our business is largely conveyed in our new Field Systems reporting segment, with key highlights on slide 9. This business is predominantly hardware, but that discrete word underplays the importance of this business to our strategy. Think of this as industrial iOT, the data collection node in the physical world that provides us the ability to connect the physical and digital worlds. In this business we are continuing to transform our selling models, moving towards hybrid models where we increasingly monetize aspects of the solution as recurring revenue, thus the segment revenue splits approximately 50/50 as hardware and software. On an as-adjusted basis, which excludes our Agriculture business, Ron Bisio and his team grew revenue by 1% while increasing operating margins by 250 basis points to 26.9%. Software, services and recurring revenue are 48% of the business, and ARR grew by 14%, evidence of our Connect & Scale strategy in motion in this segment. Market conditions remain mixed, and overall slightly positive. We see strength in the same sub-segments as AECO, including infrastructure spend. On the cautious side, we see economic weakness in pockets of Europe and Asia Pacific, most notably through lower OEM retail unit sales, and continued weakness in residential construction. We are closely monitoring US GDP growth, along with global interest rate dynamics and how that will impact capital purchases.

Closing our segment commentary on slide 10, Transportation & Logistics began the year with a solid start. We closed the Transporeon acquisition last April, thus it is excluded from the organic comparison in the first quarter. On the heels of a record fourth quarter bookings, the Transporeon team delivered a record first quarter bookings. Chris Keating and his team reorganized their go to market strategy, and recommitted to process excellence and organizational focus. They are also delivering innovation, most notably through AI driven product releases in Autonomous Procurement and Autonomous Quotation, which have found product market fit. They predominantly delivered this bookings growth in a European region that continues to experience a freight recession, thus demonstrating that selling a winning value proposition and backing it up with innovation and process improvement can generate positive results, even in a tough market environment. They also delivered a multi hundred thousand dollar annualized contract value global cross sell win, selling autonomous procurement to an existing enterprise software customer that is notably in North America. We have also begun cross selling our Maps solutions into Transporeon's European customer base. We remain confident this is an exciting Trimble business with a compelling right to win and an attractive business model that enables a series of land & expand product led growth opportunities. In context of the bookings and ARR growth, we will continue to allocate capital to our go to market expansion. In the rest of the segment, the 4% organic revenue growth was driven by our Enterprise and Maps teams, which each grew double digit. Excluding Transporeon, we have delivered consistent margin expansion since the end of 2021. Including Transporeon, the segment expanded margins by 480 basis points in the quarter.

Before I turn it over to Phil for his first call as our incoming CFO, let me once again express my gratitude to David Barnes for his service and partnership over these last few years. Phil, over to you.

Phil Sawarynski, Incoming CFO

Thank you Rob. We believe shareholder value is ultimately a function of maximizing long term free cash flow. Connect & Scale is our engine, which in the mid to long-term aims to deliver cumulative recurring free cash flow. Slide 11 highlights balance sheet and cash flow dynamics in the quarter. Free cash flow was strong in the quarter, coming in at $227M or 1.4 times non-gaap net income. We continue our asset light model with capital expenditures less than 1% of revenue and negative net working capital. Pro-forma net debt to EBITDA after the close of the agriculture joint venture stands at about 1. Post the close of the AGCO transaction, at the beginning of the second quarter, we have just under $1 billion in cash even after paying down our term debt and the outstanding balances on our credit facilities. Our strong cash balance puts us in a good position to resume our share buyback activity after we issue the 10-Q.

Now a few comments about capital allocation. Our priority remains the same, which is to invest back into our business where we see opportunities for the highest returns. For example, over the last few years we have been investing in digital transformation, the fruits of which are being demonstrated in AECO. We continue to transform our processes and systems in AECO, and over time we will expand this work throughout the rest of the Company.   As promised, we retired over $1 billion of debt in early April. In January, we announced an $800 million dollar share repurchase authorization and in the first quarter we executed $175 million dollars of buybacks.   On the merger and acquisition front, we will opportunistically pursue tuck-in acquisitions, with a bias towards the AECO segment where we can land & expand with capabilities that fit inside the Trimble Construction One offerings. As an example, we acquired a field human resources application in the third quarter of 2023, and doubled the customer count in the first few months under our ownership. This was enabled by our Connect and Scale strategy via bundled product offerings that we put in the hands of our sellers. We intend to run the same playbook as we think about our acquisition strategy going forward.

Before I turn to guidance, an update on the expected timing of the release of our 10Q filing. Our auditors, EY, informed us several weeks ago that their 2023 audit of Trimble was selected as part of the PCAOB's inspection of EY's work. During preparation for the PCAOB review, EY concluded that neither EY nor Trimble had sufficient documentation related to certain IT and other controls for revenue-related systems and processes. While EY had deemed Trimble's controls over revenue effective at the time of the 10K filing, EY's subsequent internal review over the past few weeks has changed their conclusion. Unfortunately, the result is that our 10Q filing will be delayed and we will need to amend our 10K to revise the internal control disclosures after the completion of EY's additional audit procedures. We have decided to delay our Annual Shareholders Meeting until EY has completed their work.   It is first and foremost important to note and emphasize that our auditors have not withdrawn their 2023 financial audit opinion. We are committed to working with our auditors to close this out in an expeditious manner.

With that, let's turn to guidance for the second quarter and the remainder of the year. As Rob noted earlier, we are reaffirming all elements of our initial guidance for 2024, despite negative currency moves, with some puts and takes between quarters and with prudence given that we are still early in the year and our global end market environments are dynamic.   Several factors influence our outlook for the year. While we got off to a very strong start in the first quarter, some of our outperformance came from hardware and term license revenue in the first quarter that we previously anticipated would come in the second quarter or later in the year. With this dynamic in mind, we think the best way to understand our trends is by looking at the year through a lens of first half versus second half. Overall our outlook for the first half remains consistent with what we shared with you a quarter ago. We expect that as-adjusted organic revenue growth in the second half of the year will be consistent with the first half after adjusting for the impact of the extra week in the fourth quarter.

Let's now move to our detailed guidance on slide 12. I will focus again on our as-adjusted view excluding Agriculture. Please note that we have also included slides in the appendix to our presentation that provide more information on our segment and corporate assumptions. Our prior guidance assumed that the Agriculture joint venture would close on April 1, which is exactly what happened. The as-adjusted view removes Agriculture in the historical periods, which enables looking at the growth dynamics of our current portfolio in a consistent way. Our outlook for ARR growth remains strong with continued expectations for 11-13% organic growth for the year. This is driven primarily by the expectation of mid to high teens growth in AECO ARR. Our total company full year organic revenue growth outlook remains in the 4% to 7% range. This is driven by AECO growth in the high teens to low twenties, Field Systems growth flat to down in the low single digits, and Transportation revenue flat to up in the low single digits. As a reminder, our 2024 fiscal year includes 53 weeks, which increases full year and fourth quarter revenue by approximately $85M, of which approximately $70 million is in the AECO segment. Excluding this extra week, revenue growth in AECO is expected to be up in the low to mid teens.

Our margin outlook for the year is also unchanged, with non-GAAP operating margin expected to be in the range of 24-25% and Adjusted EBITDA margin in the range of 26.5% to 27.5%. This represents year over year improvement on both measures of between 100-200 basis points. AECO margins are expected to be up by approximately 300 basis points for the year and by about 50 basis points excluding the extra week. This margin expansion reflects both the strong growth in our construction software businesses with high gross margins, while continuing to invest in support of future growth opportunities. In Field Systems, margins are expected to be down approximately 100 basis points, due to changes in customer and product mix. Finally, in Transportation we expect margins to continue to improve, with margins up approximately 100 basis points for the year, with continued margin expansion in our Enterprise, MAPS, and Transporeon businesses.

Our EPS forecast of $2.60-$2.80 is unchanged and continues to reflect the benefits of capital redeployment of the proceeds from the joint venture transaction. We have already paid down all of our prepayable debt, and we continue to anticipate that we will execute on up to $800 million of share repurchases over the course of the year. Relative to our prior guidance, EPS will benefit from lower net interest expense due to the increased cash on our balance sheet, offset by lower equity income. From a cash flow perspective, we continue to expect full year free cash flow of approximately 0.85 times non-GAAP net income. This outlook does not assume a change as it relates to expensing of research and development for tax purposes. Excluding the impact of acquisition deal expenses and the 53rd week, our free cash flow forecast for the year is roughly 1 times non-GAAP net income. Note that we expect free cash flow in the second quarter to be the lowest of the year. Second quarter cash flow is normally seasonally low, and in the second quarter we will see high acquisition related expenses related to the closing and transition costs for the agriculture joint venture, as well as higher cash taxes.

I'll finish by offering a few comments on how our guidance for 2024 breaks out by quarter. As we discussed, our guidance overall assumes that excluding the 53rd week,our as-adjusted organic growth is relatively consistent between the first half and second half of the year. For the second quarter, we expect revenue between $845 million and $875 million, which reflects as-adjusted organic revenue approximately flat year over year. As-adjusted organic revenue growth year over year in all three segments is expected to be lower than the first quarter. In AECO, these dynamics reflect the timing of term license sales, which although considered as part of our ARR calculation, are recognized up front under the accounting rules, and positively impacted the segment in the first quarter. To illustrate this point further, within AECO we recognized approximately $85 million of term license revenue in the first quarter, and in both the second quarter and third quarter we expect term license revenue in AECO to be approximately $30 million, due in large part to the normal timing of term license renewals. Then in the fourth quarter that term license revenue will increase again above first quarter levels due to the inclusion of the 53rd week and January 1, 2025 in our 2024 fiscal year which is when many of the term licenses renew. Our ARR measure evens out the lumpy nature of term license revenue, and we believe it is the best measure of growth in AECO. It is important to note that term license revenue is highly profitable, so the profitability in our AECO segment and at the company level will be highest in the first quarter and fourth quarter, and lower in the second and third quarters. In the Field Systems segment, we had strong sales of geospatial technology to government customers in both the second quarter of 2023 and in the first quarter of 2024, which we do not expect to repeat in the second quarter. Transportation revenues and organic growth will be modestly lower in the second quarter primarily reflecting reduced low margin hardware sales in our North American Mobility business. At this point, we expect that total company third quarter revenue will be similar to second quarter revenue, with fourth quarter revenue the high point for the year assisted by $85 million in revenue from the 53rd week. Operating and EBITDA margins for the year are expected to follow these same trends.

We look forward to providing you with more details on the drivers and economics of these segments at our investor day event in December.

Rob, I'll turn it back over to you.

Rob Painter, CEO

Thanks Phil.

When we think about our right to win at Trimble, we believe we can uniquely bring together users, and connect workflow, between the physical and digital worlds across industry continuums. Connect and Scale is our strategy. Our strategy is an industry platform strategy. Our platform strategy is in turn a data strategy. If we are successful in our pursuits, we will collect one of the most complete data sets in and across industries, creating a flywheel of enhanced insights and data connectivity, thereby enabling our customers to transform how they work, while building a competitive moat around our business. Thanks to all our Trimble colleagues for delivering a solid start to the year and for demonstrating resilience and conviction as we continue to transform how we work, so that we can transform how the world works.

Operator, we can now open the line to questions.