Q3 2026 Earnings Call

Company Participants

- Ivo Jurek, Chief Executive Officer
- L. Brooks Mallard, Executive Vice President, Chief Financial Officer
- Richard Kwas, Vice President of Investor Relations
- Unidentified Speaker

Other Participants

- Andrew Kaplowitz, Analyst, Citi
- Brandon Knutson, Analyst, Morgan Stanley
- Chris Dankert, Analyst, DA Davidson
- David Raso, Analyst, Evercore ISI
- Jeffrey Hammond, Analyst, KeyBanc
- Jerry Revich, Analyst, Wells Fargo
- Nigel Coe, Analyst, Wolfe Research
- Stephen Volkmann, Analyst, Jefferies
- Tomohiko Sano, Analyst, JP Morgan

Presentation

Operator

Hello, everyone. Thank you for joining us, and welcome to the Gates Industrial Corporation Third Quarter 2026 Earnings Conference Call. After today's prepared remarks, we will host a question-and-answer session. (Operator Instructions)

I will now hand the conference over to Rich Kwas, Investor Relations. Rich, please go ahead.

Richard Kwas {BIO 6934084 <GO>}

Greetings, and thank you for joining us on our third quarter 2026 earnings call. I'll briefly cover our non-GAAP and forward-looking language, before passing the call over to our CEO, Ivo Jurek, to be followed by Brooks Mallard, our CFO.

Before the market opened today, we published our third quarter 2026 results. A copy of the release is available on our website at investors.gates.com. Our call this morning is being webcast and is accompanied by a slide presentation. On this call, we will refer to certain non-GAAP financial measures that we believe are useful in evaluating our performance. Reconciliations of historical non-GAAP financial measures are included in our earnings release and the slide presentation, each of which is available in the Investor Relations section of our website.

Please refer now to Slide 2 of the presentation, which provides a reminder that our remarks will include forward-looking statements within the meaning of the Private Securities Litigation Reform Act. These forward-looking statements are subject to risks that could cause actual results to be materially different from those expressed in or implied by such forward-looking statements. These risks include, among others, matters that we've described in our most recent annual report on Form 10-K and in other filings

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we make with the SEC, including our Q3 quarterly report on Form 10-Q that is expected to be filed later today.

We disclaim any obligation to update these forward-looking statements. As a reminder, we are hosting our Capital Markets Day at the New York Stock Exchange on Thursday, November 19th. This is our first Capital Markets Day in over 2.5 years, and we're excited to share with you our strategic vision for the company. We look forward to hosting you. Before we start, please note all comparisons are against the prior-year period unless stated otherwise.

And now I'll turn the call over to Ivo.

Ivo Jurek {BIO 16343996 <GO>}

Thank you, Rich, and good morning, all. In the third quarter, we generated mid-single-digit core sales growth, consistent with our guidance and delivered strong adjusted EBITDA margin, which approached 24%. Our core growth performance was fueled by high single-digit growth in our industrial end-markets globally. Importantly, growth was broad-based with the majority of our end-markets growing.

Our performance resulted in quarterly record results for adjusted EBITDA margin and adjusted EPS. We are on pace to deliver on our financial commitments for 2026, which we have increased progressively over the course of the year. The company is in good position to capitalize on the industrial upcycle that is presently taking hold and broadening. On that topic, the industrial demand recovery continued to evolve favorably in the third quarter. Relative to the second quarter, our industrial core growth accelerated to high single digits from mid single digits.

While this was led by OEM channel strength, we also realized a nice uptick in industrial aftermarket growth relative to the last quarter. Furthermore, we were highly encouraged by the strengthening industrial demand in our North American business. Importantly, our global book-to-bill remained above one-time for the quarter. Given our performance year-to-date and current demand trends, we are raising our full-year adjusted earnings per share guidance. We now anticipate double-digit growth in adjusted earnings per share at the midpoint for the year. We are reiterating our expectation for second-half core sales growth to approximately 6% at the midpoint as well as second-half adjusted EBITDA margin to measure approximately 23.5%.

Please turn to Slide 4. Third quarter sales were approximately $904 million, representing total growth of 5.6% and core growth of 5.5%. Growth was driven by continued strength in our industrial markets. Diversified industrial sales increased high single-digits. This is end market's strongest growth since fourth quarter of 2022. Additionally, commercial on-highway sales expanded more than 20% and our sales into the global personal mobility markets increased approximately 35%.

On a regional basis, North America growth accelerated exiting the quarter, an incremental positive sign for the enterprise. Adjusted EBITDA was $215 million and represented a 10% increase. Adjusted EBITDA margin increased 90 basis points to a company record of 23.8%, translating to an incremental adjusted EBITDA margin that exceeded 40% relative to the prior year period. The margin expansion was primarily driven by volume growth, manufacturing performance, and enterprise initiative improvements, slightly offset by investments in our strategic growth areas. Adjusted earnings per share increased approximately 21% to a quarterly record of $0.47. The

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increase was predominantly driven by core growth and stronger operating performance. Brooks will address in more detail later in the call.

On slide 5, we'll review our segment highlights. In Power Transmission, sales were approximately $560 million, increasing 5.2% on a core basis. Industrial demand remained strong throughout the quarter, led by high-teens growth in Industrial OEM. Personal Mobility delivered approximately 40% growth driven by meaningful contributions from all major regions. Commercial On-Highway was also a significant growth contributor, expanding over 20%. Power Transmission delivered adjusted EBITDA margin of 24.5%, an increase of 160 basis points. Margin performance was driven by solid operating leverage on volume growth and strong operating performance.

In Fluid Power, sales were approximately $343 million and grew over 6% on a core basis. Industrial OEM demand continued to strengthen during the quarter. Commercial On-Highway increased more than 20%. Construction was also a nice contributor to the overall segment growth, growing high-single-digits. Agriculture grew slightly and increased mid-single digits on sequential basis. We are encouraged by the gradual improvement in our customers' activities across the agriculture space and are optimistic about the end market experiencing a potential steady recovery during 2027.

Our Data Center revenues increased about 2.5 times compared to last year's third quarter. In Data Center applications, we continue to expand our product offering and customer base. We anticipate to deliver material growth in this end market as liquid cooling application adoption continues to accelerate. Adjusted EBITDA margin was 22.8%, down approximately 10 basis points. Importantly, segment gross margins improved 130 basis points year-over-year, driven by volume growth and execution on enterprise initiatives, offset by investments into our Data Center growth vertical.

I will now turn the call over to Brooks.

L. Brooks Mallard {BIO 19797214 <GO>}

Thank you, Ivo. I'll begin on slide 6 and review our core sales performance by region. All three regions posted solid core growth in the quarter, driven largely by strong performance in most of our industrial end markets. Americas grew 5.2% with high-single-digit growth in North America, more than offsetting a decrease in South America. In North America, industrial OEM sales grew more than 20% and the industrial aftermarket increased high single digits. At the end-market level, diversified industrial, construction, and commercial On-Highway were the largest contributors to North America's growth.

In EMEA, core sales grew 4.6%, led by double-digit growth in the automotive aftermarket. Industrial OEM sales increased mid-single-digits, partially offset by a slight decline in the industrial aftermarket. At the end-market level, commercial On-Highway and personal mobility expanded more than 20%, partially offset by softer demand in construction. APAC grew 7.5%, fueled by double-digit growth across the industrial channels. Commercial On-Highway, diversified industrial, and personal mobility increased double digits and were the strongest end-markets in the region.

On slide 7, we outlined the primary drivers of our adjusted earnings per share growth. Adjusted EPS increased from $0.39 per share in the prior quarter to a record $0.47 per share. Improved operating performance contributed approximately $0.08 of the increase. A lower tax rate, favorable interest expense, and other items combined for

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$0.01 of growth. Unfavorable foreign exchange and other items were $0.01 per share headwind.

Slide 8 provides an overview of our cash generation and balance sheet. Our trailing 12-month free cash flow conversion was 82%. We anticipate our free cash flow conversion to increase nicely in the fourth quarter, consistent with historical seasonality. Our net leverage ratio ended the quarter at 1.8 times, improving approximately 0.2 times. We repurchased approximately $57 million worth of our shares in the third quarter. Our capital structure is strong, and we have significant optionality to deploy capital. Our return on invested capital was 21.5% on a trailing 12-month basis. Our business investments are beginning to pay dividends, and we anticipate generating higher returns on capital over the mid-term.

On slide 9, let's discuss updates to our 2026 outlook. We are reiterating our guidance for core sales growth at the midpoint and increasing our guidance for adjusted EBITDA and adjusted earnings per share. We have narrowed our full-year core sales growth to a range of 3.2% to 3.8%, maintaining the 3.5% midpoint. For the full year, we estimate total growth of approximately 5% at the midpoint. We now anticipate full-year adjusted EBITDA to be in the range of $809 million to $823 million. We have updated our full-year adjusted earnings per share to a range of $1.66 per share to $1.72 per share, a $0.03 per share increase relative to our prior guidance midpoint.

Our guidance for capital expenditures and free cash flow conversion is unchanged. For the fourth quarter, we estimate total sales to be in the range of $905 million to $925 million and core revenue growth to be approximately 6.5% at the midpoint. We anticipate our adjusted EBITDA margin to increase about 120 basis points at the midpoint.

I will now turn the call back over to Ivo for summary remarks.

Ivo Jurek {BIO 16343996 <GO>}

I'll conclude on slide 10. First, we had strong third quarter. Core growth was in the mid-single digits as expected. We generated incremental adjusted EBITDA margin above 40%, and our adjusted EBITDA margin reached an all-time record, while directing investments towards our higher growth strategic initiatives. North America inflected positively, and we are successfully managing incremental inflation.

Second, our global teams have executed well on our objectives, and we delivered on our commitments. We expect our second half adjusted EBITDA margin to approximate 23.5%, consistent with our commitment. We also anticipate to deliver record second half adjusted EPS of approximately $0.90 per share using the midpoint of our updated guidance. Our balance sheet is strong, which creates meaningful strategic optionality and we expect to lean more towards strategic inorganic investments to supplement our growth over the mid-term period. We believe the business is well-positioned to continue to deliver differentiated results. Lastly, we are excited to showcase our recent accomplishments as well as our strategic priorities at our upcoming Capital Markets Day at the New York Stock Exchange on November 19. In addition, we intend to show an array of products and demonstrations hosted by Gates' subject matter experts. We look forward to outlining our plans to what we anticipate should create significant value for our shareholders over the mid-term.

Before taking your questions, I would like to thank our approximately 14,000 associates around the world for their commitment and focus on serving our customers and

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generating solid results for our shareholders.

With that, I'll now turn the call back to the operator for Q&A.

Questions And Answers

Operator

We will now begin the question-and-answer session. Please limit yourself to one question and one follow-up. (Operator Instructions) Please stand by while we compile the Q&A roster. Your first question comes from the line of Stephen Volkmann with Jefferies. Stephen, your line is now open.

Q - Stephen Volkmann {BIO 1539931 <GO>}

Great. Good morning, guys. Thanks for taking the question. Maybe start a little bit near-term and as I think about the bridge to 4Q, you have the margin stepping down a little bit even though core growth is speeding up. And I'm curious what the offsets there are. Is it maybe some Timken dilution or spending on data centers? Just how do we think about that?

A - Ivo Jurek {BIO 16343996 <GO>}

Yeah. Hey, there's a couple of things in there. One is, we do see some normal seasonality as you move from Q3 to Q4. There's more shutdowns, there's kind of less working days in terms of manufacturing days. So, we expect to see some normal fall off of gross margin as we move from Q3 to Q4. Secondarily, as the price cost comes more into balance, we're seeing a little bit of dilution from a price cost perspective on the gross margin line as you move from Q3 to Q4.

And then lastly, as we look at our variable comp year-over-year, we're seeing a significant increase in our variable comp as we move through the full year and that mostly hits in Q4. So at the midpoint, we're about 120 bps up on EBITDA. That variable comp headwind is about 100 bps as well. So -- when you think of it from a year-over-year perspective, so we're really quite happy with our margins as we progress through the year. We think we're going to come out, as we said, 23.5% or better in the second half of the year and looking forward to continue to increase as we move through 2027.

Q - Stephen Volkmann {BIO 1539931 <GO>}

Okay, great. That's helpful. And I guess, a good problem in the variable comp side. And maybe, Ivo, switching gears a little bit, you talked about wanting to ramp up a little bit more on M&A. How do you think about M&A valuations relative to your own as you think about sort of trying to ramp that up a little bit?

A - Ivo Jurek {BIO 16343996 <GO>}

Well, sure. Look, I mean, I think that we have very high quality industrial asset that still offers tremendous opportunity for investors to generate above-market returns taking into account our financial profile and our execution. So, I'm quite happy with what we are doing on that side. And I think that the valuation is going to normalize over time as well as investors start seeing value of execution. So, look, we're going to be very disciplined. We actually do understand the reality in which we reside, and we will do deals that do offer opportunity for us to generate appropriate returns and be accretive as we execute

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them. So, we certainly don't anticipate to get into the game and get over our skis on multiples because we do understand where we reside.

Operator

Your next question comes from the line of Jeff Hammond with KeyBanc Capital Markets. Jeff, your line is now open.

Q - Jeffrey Hammond {BIO 15853475 <GO>}

Hey, good morning, guys.

A - Ivo Jurek {BIO 16343996 <GO>}

Hey, Jeff.

Q - Jeffrey Hammond {BIO 15853475 <GO>}

Just on -- so it seems like really no evidence of price cost inflationary pressures in PT, but maybe a little more in FP. Just wondering, in general, what you're seeing there and your ability to pass along, and maybe why it's a little different between the two segments?

A - Ivo Jurek {BIO 16343996 <GO>}

Yeah, Jeff, let me start here, and then I'll pass it on to Brooks. So, I would say that what I said in my prepared remarks actually on FP is not necessarily that we see inflationary pressure greater than on PT. We said that we are making bigger investments, directing investments in scaling up our strategic growth initiatives. We are investing nicely in broadening our product portfolio. We are broadening our commercial and engineering teams and getting our organizations ready to scale up our manufacturing capability and capacity.

That being said, Brooks highlighted that as the inflation is ramping up and pricing is rolled in, there is slight dilution at the gross margin and the EBITDA margin results. So, overall, I think that FP is performing just as we anticipated absent of the fact that we feel it's prudent to make the investments that we're making.

Operator

Your next question comes from the line of Nigel Coe with Wolfe Research. Nigel, your line is now open.

Q - Nigel Coe {BIO 3818998 <GO>}

Great. Thank you. Hi guys. Thanks for the question. 6.5% organic growth is a nice exit rate for 2026. I don't want to put it in the spot or anything. I know you haven't given guidance yet, but how are you thinking about '27 and any sort of early thoughts on the setup, recognizing that your're a short-cycle portfolio?

A - Ivo Jurek {BIO 16343996 <GO>}

Yeah. Look, I mean, I think that the setup is really developing quite nicely. The recovery is broadening, particularly across the industrial exposure that we have. So, we're quite

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pleased with that. We certainly anticipate that Ag should be, if not a positive driver, it will be again improved exposure over what we have experienced over the last two to three years. So, we feel that the setup is quite nice. Again, our sales continue to accelerate, right? We've gone from kind of that low single digits in Q2, mid-single digits now and expanding kind of to that 6.5% range. And so, we feel that from everything that we see, the setup is pretty decent and we will offer our first outline of how we are thinking about 2027 on November 19 during our Capital Markets Day.

Q - Nigel Coe {BIO 3818998 <GO>}

Okay, great. And then I think with the investment spending that you called out within Fuel Power, you talked about broadening the product portfolio. I'm not sure if that was data center-specific or whether it was just -- that was a broader comment, but just curious if you just maybe just kind of like go into the next level on sort of the product development pipeline for data center. That would be helpful.

And then just a quick one for Brooks. Big pickup in inventory this quarter. I'm taking that as a positive signal on demand, but just curious if there's anything else there.

A - Ivo Jurek {BIO 16343996 <GO>}

So let me start with that and I'll then let Brooks to answer the second part of your question, Nigel. Look, again, I think during the 19th of November, we are going to showcase some of the things that we have been doing. I think that you're going to see pretty significant increase in the product launches that we'll be talking about as we roll into 2027. There's a significant amount of development that is across pretty much the entire portfolio from the fluid conveyance, from the hoses side through pumps, and as well through the coupling space where we have rather significant number of new products that are coming into the marketplace.

So, we feel pretty encouraged about what we are doing from the development side. But I would say that we're also making nice investments around the commercial front end, Nigel, not just the R&D side of our house. And that should bode well with the exposure that we are building and the commercial activities that we see presently. And I'll pass it on to Brooks.

A - L. Brooks Mallard {BIO 19797214 <GO>}

Yeah. Hey, there's a couple of things going on with inventory. One is, we have definitely put in some safety stock from a raw-material perspective to make sure that we can take care of our customers from a surety of supply. As we kind of work through that, we're going to convert that into finished goods inventory through Q3 and Q4, that's going to put us, I think, in a good position to Ivo's point on liking the set-up as we move through 2027. We also see inflation in our working capital, right? And that's always one of the things during inflationary times you have to work through.

We're going to start to sunset that as we start to collect on some of the pricing related to the material inflation in Q4. That's why you see a little bit more cash conversion in Q4 this quarter as opposed to normal is that pricing collection rolling through. And that's why we still feel comfortable with our 90%-plus conversion number. So, we feel good about where we sit on inventories. From a surety supply perspective, we're going to have put nicely aligned inventories as we head into a bit of an uptick next year and feeling confident about our 90%-plus conversion as well.

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Operator

Your next question comes from the line of Jeff Hammond with KeyBanc Capital Markets. Jeff, your line is now open.

Q - Jeffrey Hammond {BIO 15853475 <GO>}

Hey, guys, good morning. Just got cut off there.

A - L. Brooks Mallard {BIO 19797214 <GO>}

Yeah.

Q - Jeffrey Hammond {BIO 15853475 <GO>}

Just --

A - L. Brooks Mallard {BIO 19797214 <GO>}

Thanks.

Q - Jeffrey Hammond {BIO 15853475 <GO>}

Back on the -- I mean, North America, it is getting better, but I'm just wondering what the drags are there still relative to rest of world, which is surprisingly growing faster. And maybe just specifically comment on what you're seeing in auto OE and auto aftermarket in North America? Thanks.

A - Ivo Jurek {BIO 16343996 <GO>}

Yeah. So let me start with the auto question. So, in North America, in particular, auto OE was down slightly, so kind of very low single digits. AR was up slightly in North America after a pretty torrid set of quarterly growth spurts that we have seen, and we believe that that's going to start reaccelerating again as we go and normalize through that large customer acquisition that we have had about a year ago. So, we feel that that's in a pretty good shape.

And I'll say that the industrial OE markets have been growing. They have been on a very, very fast pace kind of in the growth in the 20s, and IR has accelerated very, very nicely. So, industrial aftermarket has accelerated very, very nicely for us in North America as well into the low teens. So, the industrial end markets have definitely inflected very well. Auto is kind of muting little bit that growth rate, but we're in a very good shape in North America. And as I said, that revenue gen has accelerated as the quarter three progressed.

Q - Jeffrey Hammond {BIO 15853475 <GO>}

Okay. Thanks, guys.

A - L. Brooks Mallard {BIO 19797214 <GO>}

Thanks, Jeff.

Operator

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Next question comes from the line of Andy Kaplowitz with Citi. Andy, your line is now open.

Q - Andrew Kaplowitz {BIO 15179203 <GO>}

Hey, good morning, everyone.

A - L. Brooks Mallard {BIO 19797214 <GO>}

Morning, Andy.

A - Ivo Jurek {BIO 16343996 <GO>}

All right.

Q - Andrew Kaplowitz {BIO 15179203 <GO>}

Ivo, maybe just because you have an Investor Day coming up, which I know you don't want to front-run, you did lay out at your last Investor Day a series of enterprise initiatives. So, could we expect sort of a 2.0 or a Phase 2 of these initiatives? And is there any particular area of cost out that you're likely to focus on at the Investor Day?

A - Ivo Jurek {BIO 16343996 <GO>}

Yeah. Look, we will certainly provide you a window into how we are thinking about the Enterprise Initiatives 2.0. We feel quite well about where we sit with that and the opportunity that it will represent as we move forward. But I'll tell you that we are much more focusing on delivering above market growth rate. And I will say that certainly in Q3, we have demonstrated that we are growing nicely above the end market growth that we have an exposure to. So, I think that we are delivering nice gains across our enterprise, and we have spent last three or four years dealing with very negative end market macro, and we have delivered what I would say, numbers that our company and our associates are very proud of. And I believe that we can now start talking towards delivering a premium growth [ph] rate and still advancing our initiatives around profitability. So, we're very excited about what the future holds for us.

A - L. Brooks Mallard {BIO 19797214 <GO>}

Yeah. And let me just add to that. If you look at our gross margin progression and you think about when we talked about driving the gross margin improvement of the company, you've seen our gross margin steadily march up. So, we've improved our operational profitability over the course of the past couple of years. And to Ivo's point, we feel really good about the work that we've done and where we sit today, and we are super focused on growth as we move forward.

Q - Andrew Kaplowitz {BIO 15179203 <GO>}

And Ivo, maybe to your point of above-market growth, Personal Mobility has been pretty strong, had another strong quarter in Q3, I think delivering 35% growth. I think you've talked about continued double-digit growth in that business. So, maybe just talk about the visibility you have in that business going forward.

A - Ivo Jurek {BIO 16343996 <GO>}

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Yeah. Andy, we have a terrific visibility. Our team has done a great job in converting more and more end users and manufacturers in the two-wheeler space. We have nicely broadened our portfolio of products that we have. We'll be talking about some exciting things on November 19 at the CMD. So, I'll not spoil the appetite for learning more during the day. I think that people are going to be quite excited when they see what the opportunity algorithm looks for us.

We're still coming from a very small share of the market, but we are taking, I would say, significant chunks in very specific end markets and in the Personal Mobility and we believe that trajectory is open for us for a very, very long time for us as we broaden our exposure and develop products that are exciting, that people like to -- they like to adapt and they see significant value in improving the end user experience as they adapt and as we execute on those opportunities. So, while I don't believe necessarily that there is a strain line-up that's going to continue just at some analog rate, I do believe that our trajectory of kind of driving that 20% to 30% growth rate kind of over a long period of time is certainly in front of us.

Operator

Your next question comes from the line of Tomo Sano with J.P. Morgan. Tomo, your line is now open.

Q - Tomohiko Sano {BIO 16275890 <GO>}

Thank you. Hi, good morning, everyone.

A - Ivo Jurek {BIO 16343996 <GO>}

Hi, good morning.

A - L. Brooks Mallard {BIO 19797214 <GO>}

Good morning.

Q - Tomohiko Sano {BIO 16275890 <GO>}

Maybe just on data center exposures, you're already investing in data center within fully powered. What capabilities give Gates a right to win there? And what kind of customer engagement are you seeing so far? Are you already working on specific applications or new products with the customers, please?

A - Ivo Jurek {BIO 16343996 <GO>}

Yeah. So thank you for the question, Tomo. I think that we have -- we have an exposure across the full spectrum of end users and customers. We've spoken last quarter around our production ramp-up of our e-water pumps with a large manufacturer of servers in North America. We have a very nice exposure with a couple of hyperscalers on their applications, certainly are working very diligently with infrastructure builders that have been growing very nicely in the universe. And we like our exposure, but we also believe that we want to build a durable business. And we like all of our businesses. This exposure in data centers is just another incremental exposure in the industrial space where we believe we have an opportunity to continue to juice up our growth rate as we move forward.

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Q - Tomohiko Sano {BIO 16275890 <GO>}

Thank you, Ivo. And just on a follow-up, if we step back and could you talk about the NPI pipeline and then where you allocate R&D dollars as we see a strong personal mobilities and data centers, potentially some advanced robotics areas that if you could talk about how you're actually shifting or accelerating gear when it comes to NPI pipelines or R&D dollar spending?

A - Ivo Jurek {BIO 16343996 <GO>}

Yeah, totally. I think that we will speak significantly about that as we get into November 19, but we've made some anticipated expectations that we're going to get into the low-20s in NPI vitality. We are on a trajectory to deliver on that expectation as we move into the next phase of our vision here at Gates, and we'll talk more about some of the products that are coming into the pipeline, both across the data center spectrum.

I think there's some super exciting developments on the side of the personal mobility side of our business. I'll tell you, we got some really exciting things in store that we'll highlight in the industrial space in what we kind of call our legacy exposure that should offer very nice opportunity for us to capitalize on market share gains as we move into the next phase of our vision.

Operator

Your next question comes from the line of David Raso with Evercore. David, your line is now open.

Q - David Raso {BIO 1934290 <GO>}

Hi, thank you for the time. Given the significance of off-highway and industrial replacement on the FP segment, it seems like a good momentum there going into '27. Can you give us a little more color on what you're hearing from your off-highway customers, just sort of the pace of growth, where are they in inventory, the ramp up there? And also your ability to price into that market, how should we think about that, obviously, solid volume leverage, but selling to some OEMs a little bit challenging maybe on price. That's why I was happy to hear you said IR is actually accelerating. I assume that's at least a little bit easier to price into. Thank you.

A - Ivo Jurek {BIO 16343996 <GO>}

Yeah. Thank you for your question, David. I would say that the off-highway results were somewhat mixed, right? I mean, they were up kind of in the mid-single-digit range. And it's predominantly driven by construction end market. Construction was quite solid. And that was offset, frankly, by still continued weakness in Ag and our Ag was kind of flattish to maybe just slightly down year-over-year kind of think a percent down.

And so, when you think about how negative the Ag and end market is, we are quite pleased with our performance into the end market and certainly, there will be an indication that we are probably taking some market share here. So, we feel good about that and I feel certainly much better about what I believe will be a significantly improved backdrop into Ag into 2027, but my views are probably as good as anybody on the call around what's going to happen with that cycle.

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As to pricing, look, I think that we have been pretty measured in our ability to take price. We don't just price for our aftermarket customer base. We've been pretty forward-leaning in ensuring that everybody gets a price increase as inflation has been rather substantial this year as we all know, but we have been able to manage it well, and we will continue to manage through whatever comes our way.

A - L. Brooks Mallard {BIO 19797214 <GO>}

Just on the pricing too, we continue to embrace and get better at our 80-20 tools in terms of analytical pricing in terms of how we look at things. And so, I think our pricing algorithm continues to get better over time as we get better and better at the 80-20 side of things.

Q - David Raso {BIO 1934290 <GO>}

And a follow-up on the 100 bps drag year-over-year from variable comp. I'm just trying to think if I know it moves around each year depends on the performance and the metrics that are hit or not. But of that 100 bps drag, I mean, how much would you deem as a bit unique or abnormal? I'm just trying to get a sense of the run-rate margins exiting the year?

A - L. Brooks Mallard {BIO 19797214 <GO>}

Yeah. I would say this year is a little bit more normalized, a little bit up and probably last year was a little bit more down than normal. So, it's kind of a combination of both sides, both from a comp perspective, last year was lower than normal. And then, this year, I think we're higher than normal because we performed better this year.

A - Ivo Jurek {BIO 16343996 <GO>}

David, we are printing record results. So, I think that would be kind of logical that maybe the variable component of the folks' compensation is going to be a little bit better this year than it was last year.

Operator

Your next question comes from the line of Jerry Revich with Wells Fargo. Jerry, your line is now open.

Q - Jerry Revich {BIO 5626742 <GO>}

Yes, hi. Good morning, everyone.

A - Unidentified Speaker

Good morning, Jerry.

Q - Jerry Revich {BIO 5626742 <GO>}

I want to have -- Hi. Brooks, as we think about the fourth quarter, just given the outstanding gross margin performance in the third, if we just apply normal seasonality, I think that gets you above the high end of the guidance range and I know obviously we're one month into the quarter, but are there anything that -- any items that we should keep in mind in the third-quarter results relative to the fourth and that normal seasonality

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that any headwinds that we should make sure that we're mindful of given what looks like on a pretty beatable implied 4Q guide.

A - L. Brooks Mallard {BIO 19797214 <GO>}

Yeah. The only headwind is, I think we're going to be a little bit more dilutive on the gross margin side from a price-cost perspective. But as kind of some of that higher-cost inventory continues to move through the system and our pricing is all in place, you're going to see a little bit of a creep up from a cost perspective as the price-cost gets normalized. So, I would say that's the one-piece you got to watch out for in addition to normal seasonality as you move from Q3 to Q4.

Q - Jerry Revich {BIO 5626742 <GO>}

Okay, super. And Ivo, in last quarter's call, we spoke about with the margin improvement trajectory in the back half of the year, you folks are essentially in line to hit the '27 targets. As we think about the Analyst Day coming up and look forward to seeing you then, is there an opportunity to continue to drive margins higher cycle over cycle? I know you're excited about the new product side. Can you just touch on, is there further margin upside that we should be thinking about, if you could provide a teaser?

A - Ivo Jurek {BIO 16343996 <GO>}

Yeah, look, I mean, as a teaser, obviously, I understand everybody is interested in understanding what would we anticipate. But I think that we have a good set of enterprise initiatives around kind of the structural algorithm of how we run our business that we believe will continue to deliver margin expansion. But Jerry, I think that we want to think about we are starting to see some decent potential in being able to drive above-market growth rate with our enterprise. And so, we certainly believe that there's going to be a nice component of volume that's going to be driving our margin performance in addition to still a nice ability to deliver margin opportunity to our shareholders through our enterprise initiatives. So, I think that there's going to be two components.

The last three or four years, we have predominantly driven our expansion of profitability through our enterprise initiatives because again, the end markets were muted and we were just getting started with reforming our portfolio. And we feel well about where we sit with what we have been able to accomplish on that side as well as what we have accomplished on driving our gross margins performance to the record level that we are printing these days. And we believe that that's just the beginning.

Operator

Your next question comes from the line of Chris Dankert with D.A. Davidson. Chris, your line is now open.

Q - Chris Dankert {BIO 19209742 <GO>}

Hey, good morning, guys. Thanks for taking the question. My apologies if I missed it, but can you just kind of dig into the recent Belt acquisition you completed about a month ago here. Can you just kind of rightsize us on sales contribution, kind of what margin level coming on board? Any detail there would be really helpful.

A - Ivo Jurek {BIO 16343996 <GO>}

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Yeah, sure. So, we've closed it in the beginning of Q4, so there was no contribution in Q3 in revenues. And we anticipated there's going to be diminutive amount of revenue in Q4, predominantly driven by the fact that the Timken, frankly, and the customers pre-bought the inventory to ensure that there are no hiccups with these corporate carve-outs. We are ready to support our customers really nicely. I think that our teams, both of the teams on the Timken side and on Gates side have done a very good job in the transition.

And so we believe that more meaningful contribution of revenue is going to start appearing into 2027. I would say it's about 100 bps plus or minus of revenue for a company in '27 and the profitability was dilutive, certainly at what Timken was able to generate, but we anticipate that over the next 12 months or so, us -- Gates being the right owner, we certainly have a line of sight of being able to kind of get that business to company average profitability over the next 12 months. So, that's a good opportunity for us. I think it was a good transaction for the company, and we are pleased to have had the opportunity to take the assets over.

Q - Chris Dankert {BIO 19209742 <GO>}

Yeah, that's very helpful. Thanks so much, and I'll turn it back there.

Operator

Our last question comes from the line of Brandon Knutson with Morgan Stanley. Brandon, your line is now open.

Q - Brandon Knutson {BIO 24378920 <GO>}

Hi, good morning. Thank you for taking my question. Shifting to Personal Mobility, 40% growth in the quarter, really strong versus, I think you said 25% plus last quarter. What are you seeing here that's driving that acceleration? And if we look at both personal mobility and then data center, 2.5x year-over-year, how much production capacity do you have to support this? You've given like multi-year targets for both of those. So do you have everything you need to hit those or is more investment required?

A - Ivo Jurek {BIO 16343996 <GO>}

Yeah, sure. Look, I mean, I think, our mobility business has delivered terrific growth, particularly in Asia last quarter, but it was broad-based in all of our major regions. These -- we've talked about the pipeline of opportunities and the penetration that we were driving, and it's just showing up in the numbers, right? But again, I'll caution, not every quarter is going to be up 40%. Obviously, we do target that 20% to 30% algorithm over the next several years. I certainly believe that there will be periods of time where just like it was earlier in the year where we had kind of a high to -- high single-digits to teens growth and as that seasonality goes through, there are quarters that you grow 40%, 30% and so on and so forth.

So, we certainly believe that the line-of-sight that we have is that trajectory of that 20% to 30% growth rate over the next two to three years again and we'll continue to demonstrate that we can execute on that commitment. As to the capacity question, we have placed the capacity in place for support of our personal mobility business. So, we're in a very good shape there. And as I've indicated on my earlier remarks, we have been making investments into our data center initiative, and I think that maybe it was started, we are just investing in R&D.

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We are investing in R&D, we are investing in production scale up. We are adding capacity. We have some new capacity that is coming online in couple of our regions across the fluid conveyance portfolio, so the houses side, coupling side as well as incremental capacity coming out in terms of our pumps. So, I think that we are well-positioned. Again, we have been primarily focused on ensuring that we have the right portfolio so that we can generate durable and sustainable revenue into these applications over the long term.

Q - Brandon Knutson {BIO 24378920 <GO>}

Great. And then on margins, you've highlighted 100 bps headwind from variable comp in Q4 and you've also been talking about these growth investments for data center. Can you quantify the growth investments you saw in this quarter and embedded in the guide for Q4 and the impact there? Thank you.

A - Ivo Jurek {BIO 16343996 <GO>}

No. I mean we -- the investments are broad-based. I mean, some are operational and so they're more on the gross margin line, some are R&D. I would say R&D is up this quarter. In our investment in sales, the front end is up this quarter. But we don't really quantify the different pieces and the parts. The variable comp is one that we've historically covered just to equalize things out over time. But just suffice to say, it's kind of something that we're going to continue to do as we continue to improve our gross margins. One of the backbones of driving gross margin improvement is your ability to invest in the business and grow and we're going to continue to do that over time.

A - L. Brooks Mallard {BIO 19797214 <GO>}

And then and I would maybe add to that, that while we are making investments, we have built three nice businesses over the last three years organically. And I think that shareholders are starting to see the benefits of making those investments where it is not in data centers. So personal mobility will talk more about industrial chain to Belt on November 19th as well. We've built it organically without asking our shareholders to fund it. We continue to deliver on our commitments to drive profitability up, continue to deliver on cash flow generation metrics that we've committed as well as driving our gross margin performance up. And so I think that we are being pragmatic business people. We are making good investments into our own business that we believe is going to put the company on much more not only sustainable but successful path as we enter the next phase of our vision here.

Operator

There are no further questions at this time. I will now turn the call back to Rich for closing remarks.

A - Richard Kwas {BIO 6934084 <GO>}

All right. Thanks, everyone. If you have any follow-up questions, please feel free to reach out. Otherwise, have a great weekend and talk to you soon.

Operator

This concludes today's call. Thank you for attending. You may now disconnect.

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