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<<Unidentified Analyst>>

All right. Thank you, everybody. For our next company, I'm excited that Gates is holding here. It's a little newer story for a lot of people, so I think the opportunity to learn more about this company is very helpful, especially coming off their Investor Day, which I was able to attend the other day. And it's an interesting story where the company is going to evolve to and really have a great management representation here with Dave Naemura, CFO; and Bill here from Investor Relations as well. So I want to thank you both for coming, and we're here to learn. So thank you, Dave. Take it away.

<<David Naemura, Chief Financial Officer>>

Thank you. Well, we appreciate the opportunity to be here. As he said – As David said, my name is David Naemura, CFO of the company, and I have Bill Waelke with me, our Head of Investor Relations. Typical forward-looking disclaimer, safe harbor. We'll make a few forward-looking statements, but actual results may, of course, differ. I'm going to go through a quick interview. I'd love to get to questions and answers and satisfy any questions you guys may have about the business.

So a little bit of what we'll hear today. At Gates, we're the replacement folks. Two-thirds of our business comes through replacement channels, through distribution. So we'll talk about that. We have a very, very highly diversified product offering that goes into a variety of end markets and a variety of geographies. We're a market leader in most of the places we play with over 83% of our revenues coming from number one, number two or number three positions globally, and we've got a history of now two rounds of private equity ownership. But what people, I think, misconceive that, that means there's no margin expansion left for this business, and we've demonstrated tremendous margin expansion over the last few years. And we'll talk a little bit about why there's significant opportunity for further margin expansion for Gates in the future. So that's a little of what you'll hear today.

The Gates vision. This business has not historically experienced – the industries that we play in have not historically experienced a large degree of innovation, and we've reintroduced that to our products and to the markets in which we participate. And it's very much consistent with the history of Gates going back to 1911. A combination of our innovation, our brand strength, which it's a 100 year-old brand that end users have a great affinity to, and our global footprint that allow us to have the opportunity to grow at rates greater than the markets, and as a result, of course, generate strong free cash flow is associated with that.

At a glance, 2018 was a record year for Gates. We had about $3 billion – a little over $3.3 billion in revenue and generated adjusted EBITDA margins of 22.6%. We operate the business under two segments or product lines, if you will. Power Transmission, which is transmitting mechanical power between two devices, think a pulley or a sprocket. We make the device, typically a belt. It can be a toothed belt like a synchronous belt or a friction belt, an asynchronous belt to transmit power between those two devices. Or Fluid Power. And Fluid Power is everything from conveyance of fluids to hydraulic hose and hydraulic hose and premium hydraulic hose. In most cases, for Gates, premium applications is where we play, and it's where the Gates brand promise is most important, where the cost of downtime is incredibly expensive relative to the cost of the product. Both of our segments have scale and global presence and are over 60% replacement or distribution sales.

So going a little bit further into our two segments. Our Power Transmission segment, just under $2.1 billion in 2018, grew on a core basis at 3.6%, growth driven by a strong year in industrial end markets and automotive replacement channels. So we service a lot of automotive end market but through replacement channels, which is unique and has a different dynamic, and is focused on an aged car parc that is seven to 12 years old. And within that, we provide a large SKU count of replacement parts relative to the cars in that local area.

We are the number one player in the products we serve into this end market, and we've opened many or most of the emerging market territories in the world and are very involved in places like China that have a very large, growing car parc benefiting from the years of growth and registrations in recent years. I noticed that – I noted the two-thirds of our business goes through replacement markets and service a very diverse set of end markets, everything from camera lenses and ATMs to automotive – automobile applications and industrial applications as well.

The markets in Power Transmission that we participate in are highly fragmented and very large and are about $30 billion in total addressable market size. On the Fluid Power side. Our Fluid Power segment, about $1.2 billion in 2018, again driven, really, by a very, very strong year in hydraulics, resulting from many of the end markets – industrial end market strength that we've seen. About – hydraulics is probably about two-thirds of our overall Fluid Power business. Again, over 60% of the revenues in our Fluid Power business go through distribution.

Our Fluid Power business geographically is more heavily weighted towards North America, and we believe hydraulics and premium hydraulics, which is our largest category and our most competitive category, that we have a significant opportunity for further international penetration. I will talk in a minute about some of the capacity we've recently stood up. We have a new hydraulics manufacturing plant in Poland. That is the first of scale hydraulics manufacturing plant we've had on the European continent. And we completed the fit out of half of our China plant. We had half capacitized. We've now fully capacitized that plant to further penetrate emerging market opportunities in Asia

Pacific. The Fluid Power markets that we participate in, roughly similar in size to our Power Transmission market. It's about $29 billion of total addressable market.

So I keep talking about replacement channel presence. Gates – at Gates, we're the aftermarket guys. Roughly two-thirds of our business is replacement channel in nature. And fundamentally, we make mission-critical parts that are used in harsh and hazardous applications that must be replaced on a regular basis and their applications where the cost of downtime is incredibly expensive relative to the cost of the product. So you're not going to save $5 and put it into your product in there. You buy Gates. You understand the Gates brand affinity, and you ensure uptime. We kind of refer to that as the structural attractiveness of the product in the aftermarket presence, and we think it's borne out over decades of kind of proof points.

From an end market perspective, we have highly diversified end markets. This chart shows from both the replacement or two-thirds side versus the first-fit side how the end markets we address play on the replacement channel side. And then on the first – and then on the automotive side, be it replacement or first-fit, how that exposure relates to developed markets and emerging markets. And what you see is a wide range of applications across numerous end markets. About 36% of our revenues are generated from a broad set of industrial markets in the industrial replacement channels, and about 26% of our revenues are generated from automotive replacement channels.

And again, that is related to sales of applications on a car parc that's generally seven to 12 years aged. On the first-fit side of the business, we generate about 22% of our revenues from first-fit customers in construction, agriculture, heavy-duty truck and bus end markets. And on the automotive side, in 2018, about 16% of our overall business went into automotive first-fit with a pretty good mix between developed market and emerging market.

Geographical diversity of the business. We have a nice balance of business across developed and emerging economies, supported by what we call our in-region, for-region strategy. We manufacture, for the most part, in the region that we want to sell the products. Our markets are very highly fragmented, especially in emerging markets. And our global footprint allows us to serve customers locally, which is important given the structural importance of the products, and to compete with local players as well.

Getting quickly into a few of our growth opportunities. We like to address industrial Power Transmission, which, along with emerging markets, and we'll talk a minute about our Fluid Power growth opportunities. It's something we're very excited about. The left part of this slide, we talk about chain-to-belt market opportunities. The three segments here under chain-to-belt represent about an $8 billion market opportunity for us. The far left side, what we call industrial chain-to-belt, is our initiative to convert industrial chain on mobile and fixed industrial applications to a belt or a synchronous belt that we would call a Poly Chain. And then we have some unique product capabilities that allow us to compete head-to-head with an industrial chain as well as certain other industrial alternative drives but primarily chain.

The middle section here, personal mobility, is targeted applications like bicycles, eBikes, eScooters, motorcycles. And we use our carbon drive technology, which is a carbon-reinforced belt into these applications. We have 100% of Harley-Davidson as an example. We do a number of bicycle applications, and a lot of the new OE platforms are winning in emerging markets are eScooter and eBike related. And then something we call precision motion control, which we also we believe is about $1 billion market opportunity.

Think material handling, material movement, and this isn't necessarily the conveyance belts, although we do make some of that. This is the drives underneath conveyance belts and the motion to get products in one segment to another, and it's impacted by very diversified end markets. And on the far right is belt-to-belt. This is a segment of the market that was invented by Gates decades and decades ago, and we look to continue to expand our product leadership here.

On the Fluid Power side, we talk about our industrial hydraulics opportunities. Ultimately, as much share as we have being a number one, number two or number three player globally, we're still reasonably underpenetrated outside of North America in premium hydraulics. So with the new incremental capacities I mentioned in China, in Europe, we'll be able to – we should be able to gain share in these two very large hydraulics markets. We're driving innovation. We've introduced new products to the hydraulics world where, frankly, there hasn't been a lot of innovation over the last 20 or 30 years. And you'll read about in some press releases we've put out, the new MXT family of hoses, which are very innovative.

And we are a leading player across premium hydraulics, but, frankly, we didn't play across the whole spectrum. And we've introduced new products now to increase our addressable market in premium hydraulics by a couple of billion dollars. And you see a little tractor there. Well, the blue hoses were the ones we've made before, but we stopped our spec range at about 2,500 psi around there. But there's a set of premium hydraulics around the 2,000-psi range that we know make us well, which allows us to get more coverage in that premium range.

At the end of the day, the core of Gates is our material science heritage, and it differentiates us. It allows us to build belts like I've talked about, Carbon Drive that can frankly do things that other people's belts can't and allows us to compete against industrial chain where others would find it difficult, and we get to introduce new products like MXT. We're very focused on innovation here at Gates. I've been in Gates since about 2015. I joined at the same time of our CEO when we admittedly inherited a reasonably low vitality index. And that vitality index now is probably maybe getting close – it's high single digits or maybe 10% and we have a vision in the next few years of getting that up to 25% over the next two to three years, given the new technologies we've introducing – we've introduced and the product road map that we have yet to come.

And we're introducing innovation again in markets that haven't seen innovation in a while that give us an opportunity to disrupt existing markets with new processes, manufacturing processes and new technologies but ultimately should result in an opportunity for us to increase our manufacturing, the production efficiency, as well as take share with innovative new products.

Not the first time you've seen a slide like this, but we think about value creation and using our material science and R&D heritage as well as our commercial capabilities and replacement market presence as an opportunity to grow the business at a rate faster than global industrial production, and with that, translate that through to earnings growth by increasing efficiency in R&D, operating our factories more effectively and more efficiently using the Gates Operating System and then using that gross margin expansion to further invest a portion of that in sales and marketing, in R&D, consistent with driving value to shareholders.

We have delivered reasonably consistent core growth. This business was impacted in 2015 and 2016 by the industrial recession as we sell – over half of our end markets are industrial related. But given the diversified – both geographically and end market diversification of the business, you can see that, in 2015, on a core basis, we were only down 140 basis points. And in 2016, on a core basis, we grew 250 basis points. Since then, the industrial markets have recovered well, then we sought the benefits of those in 2017 and 2018.

And in 2018, we had core growth of 5.9%, and that's with a very difficult automotive first-fit market in China, and China overall, market in the second half of the year, as well as a lot of automotive first-fit headwinds coming out of Europe, which us and many others have seen given recent regulatory developments. We have a guidance that we just recently published in our last earnings call for 2019, up 3% to 5%, which we think, on a core basis, which we believe is consistent with the long-term vision we've always talked about, which is global industrial production plus a few points considering the environment in Europe and China that we've carried into the year.

So we have a strong track record of free cash flow generation. We target 100% free cash flow conversion of our adjusted net income. We tend – we have tended to increase our working capital efficiency over time. We did not have as high a conversion in 2018. We had lower conversion for us historically and was a result of two factors. One, the increased capital spend associated with building our new Fluid Power hydraulics facilities, and two, on a gross basis, not a core basis, we grew the business 10.1% in 2018. And we've provided significant amount of working capital associated with that growth. We have a very high working capital requirement, around 25% of sales. And although we try to make that a little more efficient every year by about 50 basis points,

we still have to provide a lot of cash flow associated with sales. We think those things normalize in 2019, and we see our conversion being greater than 80%, returning towards historical levels.

Our capital expenditures will come down from the $180-ish million in 2018 to about $150 million in 2019. And we've always said this business should run at about 3% of sales of capital with about half of that being maintenance and half of that growth. And we'll work our way back towards that over the next – we'll probably get back there over the next year or two. We've demonstrated – well, Ivo and I have always said we'll always do what's right for the business from a capital deployment standpoint and investing to grow the long-term benefit of the business while being mindful of deleveraging.

And I think we've demonstrated that well over the last few years, a reasonably balanced approach to capital deployment. We invested significantly in the plant capacity that we needed to continue to grow with the industrial end markets. We have done three M&A deals over the last two years, deployed about $160 million of capital in 2017 and 2018, but we've consistently deleveraged. We started our journey – the original LBO of Gates was over seven times net leverage. At the end of 2015 – sorry, at the end of 2017, it had been – the leverage have been reduced to 5.1 times. And use of the IPO proceeds in January of 2018, plus an additional $150 million of cash on hand, has helped us get down to 3.4 times net at the end of 2018. And we've stated that, based on our outlook and our improvement to free cash flow conversion, we would anticipate net debt being below three times – sorry, leverage being below three times on a net basis at the end of 2019.

So from a long-term target perspective, we talk about $4 billion plus in the three to five-year time horizon. And the $4 billion plus is really consistent with our mid-single-digit view of the world that's based in global industrial production plus a few points, the plus a few points driven by our large organic growth initiatives that provide us the ability to grow faster than the market. If we grow, we should continue to expand our adjusted EBITDA margin we reflect here is greater than 24%. Implied in the guidance for 2019 is 23%, which is 50 basis points approximately improvement over 2018. And we also have an internal measure of ROIC, which adjusts for the LBO intangibles of fair value in the balance sheet. And when you adjust for that, the reasonably cost in calculation, this business should continue to deliver, if you will, intangible ROIC of over 20%.

So quickly summarizing, we're the replacement-focused folks. We don't have to be on first-fit applications to win the aftermarket, and we behave accordingly. We're highly diversified across a number of end markets, geographies and applications. And we have organic growth that's fueled by innovation and positive long-term secular growth trends. So we believe all of these reasons result in Gates being a compelling opportunity.

We appreciate your time and happy to take any questions.

Q&A

<Q>: I've got a first one. Given your opportunity, especially outside of North America for fluid, when I think about the growth profile, the three to five-year target, less than a 5% sales CAGR. I guess my first question is what do you assume for the end markets in that $4 billion guide? And if you could help us in detail, give us auto and industrial replacement, auto industrial first-fit.

<A – David Naemura>: Implied in the three to five-year guide of $4 billion plus, I think if you do the math, you would say it implies a CAGR of somewhere between 4% and 6%. So I think it really…

<Q>: 4.9% to be exact. But what's the end rolling market is what I'm trying to get at.

<A – David Naemura>: I think we see two to three points of positive global industrial production, plus a few points beyond that. I think automotive first-fit, for us, is probably a flat business through the cycle. We've turned down more business in automotive first-fit than we take. We're not really a true market participant. We – therefore, the market may grow. It's less our objective to grow the first-fit component of our business more to stay relevant because it is a reference for our aftermarket business. Therefore, that goes down from maybe 16% in 2018 to 15% or 14% to 2019. It continues to decline a little bit. We think the industrial markets probably don't grow at the rate they had been growing but remain reasonably healthy. But we have to drive a couple of points above that, and that's the opportunity for the hydraulics expansion, and frankly, chain-to-belt.

And if we think of the big three growth drivers, one, one-third of our business is in emerging markets. And we believe emerging markets are a double-edged sword. But we believe emerging market presence gives us an opportunity for outsized growth in things like the Chinese automotive aftermarket, which, given the rate of registration growth over the last number of decades, there's a positive tailwind to the automotive aftermarket development in China for, again, decades to come. Emerging markets is one component, the hydraulics expansion, both increasing our product range as well as international penetration as well as new product. And then that's now, and we're really seeing that kick in as we've launched MXT and got the new capacity online.

That should fuel growth over the next few years. And the largest opportunity is clearly chain-to-belt, going after that $8 billion of addressable kind of greenfield segment for us,

but that will be longer term. So the combination of those three initiatives is why we think we would get a couple of points above the market. Price cost is also kind of in the calculation. Price cost was very favorable for us in 2018, and we think that will be less so. We think 2019 is less of a pricing environment but also less of a raw material environment, inflation environment. We always look at price as an opportunity to offset raw material inflation. We've successfully done that, and that's kind of how we think about price so some additional detail there, I guess.

<Q>: Actually wait for a mic. I apologize. One second. Chuck, over here.

<Q>: Thank you. On the auto side replacement, how much of that is warranty versus non-warranty replacement? And maybe just talk about kind of from a channel standpoint, how much is dealer versus independent globally?

<A – David Naemura>: For us, this is independent. And this is – really, when we say automotive replacement, we're talking independent out of warranty. So we target the independent mechanic. Our parcs tend to fail, again, in that seven to 12-year time frame, so outside of when is repair to the dealership. Because we – North America is a good example. Less than 2% – around 2% of our revenues come from automotive first-fit in North America where we have 65%, probably, of the aftermarket business in North America. And so we really disassociate our aftermarket business from the OE application, and we're going to win the independent in that seven to 12-year time frame.

<Q>: Just to make sure I understand that. When you put up those market sizes, are you talking specific to those market sizes replacement or specifically non-warranty replacement?

<A – David Naemura>: There might be something in there, but I would say it's 99% non-warranty replacement.

<Q>: Okay. Thanks.

<Q>: If I can just follow up on that. So you said out of that 16%, 2% is U.S. Can you kind of break down the other 14%?

<A – David Naemura>: About half of that 16% is going to be emerging market with China being the biggest component, roughly. Roughly half of our emerging market exposure will be China. And then the largest developed market, if you will, eight points, roughly, is developed. The biggest component there is going to be Europe, which is a very large synchronous market. And then beyond that, kind of Japan probably. Korea, I

would put – Japan and Korea are big markets, so I would Korea in the emerging market, I think, by our definition. But China and Europe are the big markets for us.

<Q>: I have a quick question. I know you said leverage in a few years less than three, so it could be two, 2.5. But when I think of you at 3.4, to get down below three, your EBITDA this year is, roughly, call it, $800 million. So 1.4 turn is only $300-plus million, $320 million.

<A – David Naemura>: Yes.

<Q>: If you're going to generate – let's say your numbers are right, you're doing $3.5 billion, up to $4 billion of revenue a year, your free cash flow every year should be at least $300 million, $400 million. So you say less – I mean, you should easily be less than three. Is there any other need for the free cash flow besides less deleveraging right now. That's the…

<A – David Naemura>: No specific need, and we are focused on deleveraging. But we also think M&A can be a very important part of the story here. So I think what we've said is our opportunity for M&A probably get to a little more – we get a little more latitude as we get below three times. Is two times is the right leverage for this business? Probably some day. But we think given the highly fragmented nature of the markets and our ability to add value to a deal through both innovation, our technology application to Gates Operating System, replacement channels, that M&A could be an opportunity. So we've always been focused on three. And for now, that's the milestone. I think we're committed to getting below.

<<Unidentified Analyst>>

All right. We're about out of time. So if anybody has the last question, raise your hand. Otherwise, I think we'll call the presentation. All right. Well, thank you very much.

<<David Naemura, Chief Financial Officer>>

I appreciate that.

<<Unidentified Analyst>>

Definitely appreciate it, Dave and Bill. Thank you.