Deane: Good afternoon, everyone. It's Deane Dray, Senior Analyst, RBC Multi-Industry sector. We're delighted to host Gates Industrial Corporation as our next presenter, and even more delighted to have Ivo Jurek, CEO, present. I've known Ivo for a number of years. He's got a great story to tell here. Ivo, thank you for joining us today.

Ivo: Thank you very much for the invitation, Deane.

Deane: You know, we were just talking before we went live that we wish we could be doing this in person, but it'll just make that opportunity for the live meeting in person that much sweeter when it actually gets to happen. We've only got 30 minutes. There's a lot of ground to cover. You've got an exciting story to tell.

If I had to boil it down into what investors have been most riveted on, it's been the pace of debt paydown – that's been one of the big positives – and how well you've managed price cost in what has been a horrifically challenging environment, continues to be a challenging environment. Let's just start first on price cost. Everyone's getting asked about this. Give us a sense, on a triage, how you've handled it, where the pain points are, labor shortages, how you're getting through all this.

Ivo: I think it's a good way to start, Deane, because as you know, the demand environment is very robust, and we've been clearly demonstrating that through our results over the last two to three quarters. As we exited Q2, we continue to say that we see positive book to bill. I said on my call actually that we're actually being limited through constraints, be it labor or be it material supply chain related constraints.

And that obviously brings into foray inflation when you're operating in an environment that is so dislocated in terms of supply to demand out of balances. It puts lots of pressure on inflationary factors. Taking into account the strong brand that we have and very large presence in replacement channels, we are able to react to inflationary pressures with pricing quite effectively.

We have demonstrated in 2018, and certainly we have demonstrated that in the beginning of 2021. We were very early in bringing price increases into the marketplace when we have seen inflation starting to creep in, and we had to do it on a number of occasions this year. We've gone to take our prices up on more than one occasion throughout this year so far.

And by the way, we don't anticipate that that is going to change. Inflation remains pretty significant in the operating business, and we continue to believe that we'll have to be very proactive on the pricing side. We don't see any inflationary signs

that are fading, so as I said, we believe that the input cost flows remain being very challenging from all aspects – material, labor, logistics, and distribution.

Deane: Talk about pricing power here. The expectation is if you think about the stratification of competition, there's always good, better, best. Gates has always been positioned as best. There's that economic principle that says big dog eats first. If you've got the premium brand and the biggest market share, you tend to have pricing power. How is that actually translated through this time in this environment?

Ivo: I would put it a little differently maybe, maybe not as eloquently as you, but we are top three market participant across the entire product line segments that we operate. We view ourselves as somebody that sets price that does not react to pricing. We, taking into account the significant inflation as we've discussed, that we have seen this year, we have taken pricing action across both of our businesses on a first fit side just as much an on the replacement side of our business.

Generally speaking, the aftermarkets, they operate kind of on a 90-day notice period. We think that we are able to react very effectively to inflation that creeps in. In '21 we've taken a number of pricing actions, as I said during the prior question segment. With respect to OEMs, some have some material, raw material passthrough clauses, and so obviously that's beneficial on the upside as well as on the downside. It makes it easier to maybe take price to those customers and we have been able to certainly enact those.

We have really not discriminated versus OEM or distribution channel partner. Inflation has been significant, and we have taken a significant price into the channel or into both of these channels a couple of times this year. Again, as I said, we are a large market participant and a significant market share holder, and we believe that we will set pricing rather than follow somebodies pricing actions.

Deane: Ivo, you said something really interesting. Just make sure I understood it correctly. When I think of OE relationships, those you're kind of, you're spec'd into a product that has a longer duration in terms of the period under contract, whereas distributors are much more hand-to-mouth, short duration, and distributors are actually eager to take on price, most typically, because they get a markup. Better to have a markup on a higher priced product than lower. Maybe just to clarify the OE versus distributor pricing approach.

Ivo: Absolutely. I mean, again, you said it correctly, distributors don't dislike pricing. They do, generally speaking, have the ability to take that into the shelf pretty quickly. They update their price books electronically or physically in catalog. That window is, generally speaking, kind of 90 days. You go in and you announce

your pricing and within 90 days, you've been able to take that price into the marketplace.

The OEMs, they have a longer-term contract, and generally speaking again, it is much more difficult to reset prices based upon the contractual agreements that you have in place. Again, the inflation has been pretty significant, as you probably hear from all of your companies in the coverage. We have been able to get pricing through the OEM channel as well. Although it's much more difficult of a task to do, we still have been able to do that this year.

Deane: That's really good to hear. Let's pivot away from the price/cost side, which, again, from the opening, you all give the appearance of managing this very well. It's very transparent. You've communicated it, so really appreciate that. The other side point is on paying debt down faster, which is such a positive because it signals good balance sheet management, good cashflow, etcetera. Take us through where it stands today, the path of the debt paydown, the sweet spot where you want to be, and capital allocation priorities overall.

Ivo: Deane, as you said in the opening, you and I have known each other for some time, and you certainly have been with us since the beginning of our life in the public space from 2018 on. My number one priority, communicated priority has been the fact that I felt we needed to deleverage our business. We are a high-quality industrial asset. We felt that to be viewed as such we also needed to be levered, our leverage needed to get more in line with our large industrial peers.

We have taken, we have undertaken a process where we felt that over midterm, we wanted to get to 3X leverage. We've actually been able to get to 3X leverage a little bit faster than we originally anticipated. We have gotten to 3X leverage, just slightly under 3X leverage, at the end of Q2, and we have set our objectives a little bit higher now. We felt that the place where we feel comfortable residing is somewhere between 2 to 3X through the cycle, and so now we're on a trajectory to go and reach that 2X leverage over the near-term.

Absent of doing something out of ordinary throughout the remainder of the year, we will make incrementally nice progress towards that 2X leverage target by the end of this year. We believe that we're in a very good shape leverage-wise, we feel very comfortable residing in the neighborhood of 2 to 3X leverage, but again, we are generating tremendous amount of free cashflow, and the fact that we are below 3X levered, now also opens up the way for us to be able to look at deployment of that excess cashflow into an inorganic set of initiatives if we find some that we believe will be accretive our business and would generate reward for our shareholders.

Deane: Ivo, that solved, that kind of begs the question is what's the funnel look like, what's the pricing look like, what makes sense in terms of where and how do you add to the portfolio?

Ivo: I always start with the way that I try to approach M&A. I says, look, many companies are changing their approach and maybe that's a reaction to the multiples that they have to pay. We believe that we frankly need to generate double-digit ROIC over the first three years post-acquisition, and we will not shift away from that.

We believe that, I mean, it will require that you find assets that you can buy at a high quality for a reasonable price. We're not intending to be paying significant premiums to multiples that we see today, so assets and expenses today, as you know. We're also participating in a very large market and our market is very fragmented. Not all assets in that space are trading at significant premium to fair market value.

We do have a good buy plan of opportunities. We're working a number of bolt-on acquisitions that we believe would help us to accelerate our strategy, and we will pull the trigger as long as we can stay within that constraint that we have put on ourselves, which is double-digit ROIC in the first three years post-acquisition.

Deane: That sounds exactly the way investors should want you to use the balance sheet and if you see those. There are assets out there, targets out there that you believe would fit that criteria.

Ivo: Yes, we have number of assets. We actually continue to build that pipeline. We have been cultivating the pipeline, as you know, Deane. We have a group within Gates that is tasked with building the pipeline and, you know, there are a number of interesting assets out there that we are looking at presently, but again, we will be disciplined. That cash is not burning the proverbial hole in our pockets in here.

We still have a good set of opportunities to deploy our excess capital, either through a debt paydown or we'll look at some other alternatives that may be better in terms of rewarding our shareholders. We'll be patient. We will continue to build a pipeline and we will pull the trigger when we believe we can get those deals done at the prices that we feel are fair prices.

Deane: Let's circle back to the top line, and Ivo, I took careful note that in your opening comment you said that demand remains robust. Is that still the case? Just take us through the extent that you're comfortable talking about end markets and would love to start there.

Ivo: I'll come back to the Q2 earnings call where we reaffirmed that our book to bill remained solidly north of one. We certainly have seen very strong underlying demand for our products. We don't have anything outside of that to share with the public presently. We feel very good where demand resides. I think I might have also said that the demand is very strong, inventories are very lean, but we are all dealing with supply constraints.

The supply constraints in my mind are bifurcated into two camps. One is labor, predominantly in the United States, and the other one is raw material, and the raw material not only impacts our ability to manufacture products, but it also sometimes impacts the demand for our products at our customers. I think that we have been pretty conservative in terms of how we have provided guidance, taking into account these constraints.

These constraints are not going away. They're not abating. They certainly have almost intensified, if you would, but we have managed well in Q2, and we continue to manage and deal with these constraints as we deal with them on day-to-day basis.

Deane: Did I hear you say you'd characterize the labor issue as mostly a US phenomenon?

Ivo: Yes, Deane, it is certainly for our side of the business. We are in places where we don't seem to have a difficulty finding labor with the exception of the United States. I think the United States we are dealing with some different dynamics. We are dealing with the COVID dynamic that has come back again. It's quite significant.

We did see a pretty significant set of infections go through certain segments of the country, and I think the issues associated with the unemployment benefits and some of the relief that the government has enacted probably has an impact on labor participation rates. I'm certainly hoping that it will work itself through as we exit 2021, but my sense is that we'll continue to see very tight labor markets in the US through the remainder of this year.

Deane: To stay on that theme, because that was really helpful, how is COVID change or has been changing demand in your markets, and is there anything that's going to be a permanent change, just kind of like that has either accelerated trends, but how do you characterize what you've been through, other than just making it difficult if people come to work? What's happened to demand and secular trends?

Ivo: I think, Deane, you are right. We are seeing very strong secular trends in number of our end markets. In diversified industrials as an example to start with, we're seeing very strong momentum in industrial automation, particularly in

warehousing, logistics applications, with acceleration of ecommerce, and precision motion control applications such as robotics. Anything that can kind of overcome some of the issues that we just talked about, the availability of labor participation and the ability to operate 24/7 by uninterrupted means.

We see really strong trends in mobility and recreation. We are seeing tailwinds from the increasing micro mobility trends where people look at trying to gain more independence with their commuting transportation, and frankly, fitness options. It's great to go to a gym. I used to love going to the gym, but I can tell you it is a lot more convenient for me to go down to my basement and jump on a couple of pieces of equipment and I still can be in the office at 7 am and get back to work rather than commute from point A to point B, go to a gym, and then try to get back to my office.

I think that people see that as an optionality that is convenient for them, and that is a really strong tailwind for us, particularly in that micro mobility segment of our initiatives-driven growth. We're also seeing some strong fundamentals in our automotive replacement side of our business. The car parc continues to get bigger. It ages. The fact that people have been driving, they're not maybe driving to the office, but people are driving back, miles driven are back into pre-pandemic levels.

When you combine that with aging car parc, car parc getting older, people driving lots of miles, inability to get a new car, hey, you know, that's a good solution for our large and very profitable automotive replacement business.

Deane: Let's talk about that. I love how you said, when you talk about auto, it's the auto replacement business. Maybe just briefly talk about first fit, and I always like hearing that you, if this is still the case, that you pass on more OE/first fit business in auto than you actually take on, that you're managing what percent of auto exposure OE versus aftermarket. Take us through that, the economics and where that stands today.

Ivo: Fundamentally, we are a replacement-focused company. We've stated that from the get-go nothing's really changed. Our brand, our reputation for quality leading product range coverage means that we don't really need the first fit as a supplier to capture the aftermarket. It's actually the opposite. We really don't pay any attention. We have strategically de-emphasized, since the IPO, our automotive first fit business, focusing much more resources on the higher margin, more stable replacement channel.

We do continue to very selectively, to your point, very selectively participate in first fit programs, but only where our new technology and innovation differentiate our products, particularly when we go after full hybrid or EV applications. As you

said, we turn down significantly more business than we take on. We are very disciplined. We can have our automotive first fit business four times the size, but we really have no interest in building it out.

Deane: The other question is the whole opportunity in EV and the dollar content on EV versus internal combustion. Where does that stand and what are the key takeaways?

Ivo: Obviously we could spend quite a significant amount of time on this particular question. It is something that we're actually quite excited about, and in general, we are significant, we are seeing a very significantly larger content opportunity on electrics, with the emphasis on thermal management system, where we are a key player today, primarily in ICEs and in hybrids.

When you think about the content, the content shift for us from PT to fluid power on EVs, and it is driven predominantly by dramatically more content in terms of modular hoses and with electric water pumps. The shift from ICE to EV is dramatically net positive for Gates as it relates to total dollar content. As an example, a mechanical water pump on a traditional ICE vehicle sells for about $10 to $15 per unit, while an electric water pump that is on an electric application sells for approximately $100. You see a very significant step up.

It's driven by functionality and output. Whereas ICE water pump may be 30, 40, 50 watts, the EV water pump may be 200 watts to 1.2 kilowatts, so a more sophisticated and higher output pump. It is very similar situation in terms of the thermal management hose assemblies. The content is growing for us from a content on ICE of $15 to $30, to $100 to $200 range on electrics. Net-net, we kind of see that $150 net positive content growth per vehicle on EV versus on ICE. I think very important to add is that we manufacture these products today. We participate in that business today, both on ICE, on hybrids, and on EVs.

Deane: And you know we could go further on this, but that's the bottom line that I think investors need to hear, is this is an opportunity, it's not a threat on the EV, and I think you really drove that point home. The other topic I want to make sure we touch on in, sometimes it's this from chain to belt conversion and in some cases, you'd think that this is a longer-term trend and you're never quite sure about where it actually gets traction, but it's really happening and it has surprised me to the positive on how quickly it went from, hey, we're in engineering discussions to we're booking orders.

Where is this in terms of the total opportunity for the company in this chain to belt conversion?

Ivo: I think, Deane, I always love the attention to real nuances that you put in in our business, and we really appreciate that. Coming back to chain to belt, over the last several years, I have talked over several or numerous design wins that we have been able to secure, and as you said, we are turning those design wins into billings and revenues today.

As we have reported on the last couple of earnings calls, we actually are seeing very strong growth in terms of that chain to belt initiative. This is a very steady and very long-term opportunity for our business that, frankly, will support the objective that I have put out for the company, which is we want to outgrow the industrial end markets. Mobility is some of the areas that we are targeting today, but we are also very much focused on diversified industrial chain to belt conversions and applications across the warehousing, distribution, and light industrial automation applications, to name a few.

We discussed our expectations of over $200 million of revenue and growth over the midterm in our diversified industrial end market. A large portion of those are coming from the chain to belt initiative. We are very quickly approaching the point in time that we're going to say, hey look, our first and immediate objective has been accomplished. We are now not only in a stage where we have demonstrated that we can do that and that there's actually fundamental value for the end users in switching from industrial chains to belts, but we now can start building on that foundation and continue to accelerate those conversions well into the future.

As we said, Deane, it's about a $5 billion+ market size opportunity. We are competing against non-traditional competitor there, industrial roller chain, and we believe that we should have a sizeable market share in that market over the next couple of decades. We feel really good where we are today. We are very early, but we also believe that we have demonstrated that it is not only feasible, but it is a very good initiative for the company, secular in nature, and we will continue to deliver that growth steadily over the near-term future.

Deane: We only have a couple minutes left, literally. What should we know about ESG, what the opportunity is, and what mandate and what's changing for you all in terms of how you're presenting yourself to the ESG community? Again, we only have two minutes.

Ivo: Sustainability is at the core of everything we do, and if you were to think about that, sustainability, frankly, is the core of our innovation and our production system. Our new products that we are launching are more environmentally friendly, they use more environmentally friendly materials, contain less material overall, and leverage more efficient processes. Furthermore, I will say that our

product support efficiency and sustainability improvements also at our customers in their equipment in their operations.

We are helping, we are facilitating an ability of our end users to frankly get almost a free ESG benefit by switching into more efficient products from Gates. I would also reference our recent sustainability report that we have published which highlights the overall efforts and it provides key metrics on the significant progress that we have made in terms of reduction of emissions, water consumption, energy consumption, and many other metrics like health and safety.

ESG for us is at the core of everything that we do, and it is an accelerator in some of the key initiatives such as chain to belt, as we just discussed, of the fundamental benefits that we offer to our customers.

Deane: Ivo, that was a fabulous summary of an extremely important topic that we know is important to you and important to the board. We're out of time. We went through a ton of material, so I appreciate your succinctness in allowing us to cover a lot of ground. I wish you and the whole Gates team continued success. Thank you very much for participating in our RBC conference, and with that, we will call this presentation to a close. Ivo, thanks for joining us today.

Ivo: Thank you, Deane.

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