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Gates Industrial Corp. Plc (GTES)

Q3 2025 Earnings Call

CORPORATE PARTICIPANTS

Rich Kwas

Vice President, Investor Relations and Strategy, Gates Industrial Corp. Plc

Ivo Jurek

Chief Executive Officer & Director, Gates Industrial Corp. Plc

Lawrence Brooks Mallard

Executive Vice President & Chief Financial Officer, Gates Industrial Corp. Plc

OTHER PARTICIPANTS

Nigel Coe

Analyst, Wolfe Research LLC

Deane Dray

Analyst, RBC Capital Markets LLC

Julian Mitchell

Analyst, Barclays Capital, Inc.

Jeffrey D. Hammond

Analyst, KeyBanc Capital Markets, Inc.

Andrew Kaplowitz

Analyst, Citigroup Global Markets, Inc.

Tomohiko Sano

Analyst, JPMorgan Securities Japan Co. Ltd.

MANAGEMENT DISCUSSION SECTION

Operator: Ladies and gentlemen, thank you for standing by. My name is Krista, and I will be your conference operator today. At this time, I would like to welcome everyone to the Gates Industrial Corporation Third Quarter 2025 earnings conference call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions]

Thank you. I would now like to turn the conference over to Rich Kwas, Vice President of Investor Relations. Rich, the floor is yours.

Rich Kwas

Vice President, Investor Relations and Strategy, Gates Industrial Corp. Plc

Greetings and thank you for joining us on our third quarter 2025 earnings call. I'll briefly cover our non-GAAP and forward-looking language before passing the call over to our CEO, Ivo Jurek, who will be followed by Brooks Mallard, our CFO.

Before the market opened today, we published our third quarter 2025 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 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 have described in our most recent annual report on Form 10-K and in other filings we make with the SEC, including our Q2 quarterly report on Form 10-Q that was filed in July of 2025. We disclaim any obligation to update these forward-looking statements. This quarter, we will be attending the Baird Global Industrial Conference, the UBS Global Industrials and Transportation Conference, and the Goldman Sachs Industrials and Materials Conference, and look forward to meeting many of 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

Chief Executive Officer & Director, Gates Industrial Corp. Plc

Thank you, Rich. Good morning, everyone, and thank you for joining our call today. Let's begin on slide 3 of the presentation. Gates posted solid third quarter results with positive core revenue growth of almost 2% under macro industrial demand conditions that remain subdued. Our replacement channel grew low single digits, supported by mid-single digit growth in automotive replacement. Our OEM sales were relatively flat. At the end market level, industrial was mixed.

Globally, off-highway realized positive growth with stabilizing demand in construction, offsetting incremental weakness in North American and European agriculture. Commercial on-highway declined mid-single digits impacted by decreasing production rates in North America. Personal mobility generated another strong quarter of growth exceeding 20% year-on-year. Our adjusted EBITDA margin increased nicely year-over-year to 22.9%. We generated record adjusted EBITDA dollars and margin for a third quarter. Our net leverage ratio declined to 2.0 turns, a 0.4 turn reduction compared to last year's third quarter.

With that, we are on pace to reduce our net leverage to under 2 times by year end. We have updated our 2025 guidance, raising our adjusted EPS midpoint to \$1.50 per share. We have maintained our full year 2025 adjusted EBITDA midpoint of \$780 million while slightly lowering our core sales growth outlook at the midpoint. Brooks will provide more color and comments about our updated guidance assumptions later in the presentation.

Additionally, our board recently approved a new \$300 million share repurchase authorization that will expire at the end of 2026. The new authorization replaces the prior authorization, which had over \$100 million remaining.

On slide 4, we have heard from a number of you on the call that you would like to see an update on what is occurring in the end markets. So we have laid out an updated view of our underlying end market and how they have progressed during 2025. Coming into the year, we did not anticipate a broad macro recovery, but we have continued to see uneven end market performance since we set our initial expectations for the year in February. We did, however, enter the year with some expectations that the PMIs could begin to recover in the second half of 2025. That has not emerged to date.

Industrial off-highway demand trends have continued to languish and soften a bit relative to our expectation during the third quarter in certain geographies, on reduced build rates and dealer inventory destock. Additionally, in the on-highway end market, the North American commercial truck production levels deteriorated as the third quarter evolved. Despite some of these near-term headwinds, we are still outperforming our underlying markets and believe that many of our challenged end markets are troughing or are close to troughing.

Our automotive replacement and personal mobility business continues to grow nicely, while our data center opportunity set continues to expand. As such, we are optimistic that demand in the majority of our end markets will be more stable to improving at some point in 2026.

Please turn to slide 5. Third quarter total sales were \$856 million, which translated to core growth of 1.7%. Total revenues grew 3% and benefited from favorable foreign currency. As I have highlighted earlier, the end market performance was mixed in the quarter. Personal mobility continued to trend nicely higher, with its year-over-year growth rate accelerating compared to the second quarter. Off-highway grew mid-single digits with growth in construction and agriculture globally. However, ag declined incrementally in both North America and Europe.

Diversified industrial and energy were both down slightly and on-highway demand was soft. Automotive grew low single digits, with solid growth in auto replacement more than offset a slight decline in auto OEM. Our key growth verticals, personal mobility and auto replacement contributed to the performance. Our revenues from data center also continues to increase, although from a small base. And we see the liquid cooling opportunity in early stages of more broad-based adoption.

Adjusted EBITDA was \$196 million, with adjusted EBITDA margin coming in at 22.8%, an increase of 90 basis points and representing a record third quarter margin rate for the company. Our adjusted earnings per share was \$0.39, an increase of approximately 18% year-over-year. Operating performance contributed \$0.02, while a lower tax rate and consolidated mix of other items each contributed \$0.02. We believe we are effectively managing the enterprise across all aspects.

On slide 6, we will review our segment highlights. In the power transmission segment, we generated revenues of \$533 million in the quarter and core growth of 2.3%. Most industrial end markets realized growth. Personal mobility continues to be a strong contributor, with growth exceeding 20% in the quarter. At a channel level, replacement grew with automotive and industrial channel core growth, each growing low single digits.

OEM sales also grew low single digits with industrial sales growth more than offsetting a decrease in automotive. We continue to invest in our strategic sales initiatives and innovation to help drive potential outgrowth in the future. Our mobility opportunity pipeline is staying robust.

In the fluid power segment, our sales were \$322 million, representing core growth of just under 1%. Many of our key end markets in fluid power continued to experience various levels of demand pressure, but our teams have held its own. Commercial on-highway sales decreased mid-teens as industry inventories are elevated. Off-highway grew with positive construction trends, offsetting a low single digit decline in ag. The agriculture performance year-over-year was worse, impacted by incremental OEM production cuts to better align our customers' inventory levels heading into the year end.

We believe the underlying ag market is troughing and should be better positioned for recovery sometime in 2026. Replacement demand was strong, driven by double digit growth in automotive replacement globally, with broad based growth across regions. Industrial OEM sales declined mid-single digits on a core basis, driven by soft demand trends in agriculture and commercial truck. Our data center opportunity pipeline exceeds \$150 million and design in activities remain robust. With respect to profitability, both segments expanded adjusted EBITDA margins at a similar rate.

I will now pass the call over to Brooks for further comments on our results.

Lawrence Brooks Mallard

Executive Vice President & Chief Financial Officer, Gates Industrial Corp. Plc

Thank you, Ivo. I'll begin on slide 7 and review our core sales performance by region. The majority of our geographic regions generated core growth in the quarter, highlighted by EMEA's return to growth. In North America, core sales were about flat. The incremental demand weakness experienced in agriculture and commercial on-highway during the quarter was primarily concentrated within the North American region and led to a low double digit decline in industrial OEM sales. Industrial replacement sales were also down slightly. Industrial was offset by growth in automotive, as automotive replacement sales increased high single digits, supported by year-over-year growth contribution from our new channel partner. Automotive OEM sales grew low single digits.

In EMEA, core sales grew 2.6%. Industrial end markets were mixed, construction returned to growth and more than offset weak demand in agriculture. On-highway grew while energy and diversified industrial saw declines. Personal mobility was very strong, growing almost 75%. At the channel level, OEM sales grew high single digits supported by construction, on-highway and mobility, partially offset by lower automotive OEM. Sales and replacement channels increased slightly.

East Asia and India posted approximately 5% core growth. Most industrial end markets grew. Automotive OEM sales decreased slightly, which was more than offset by high teens growth in automotive replacement. China core sales expanded 6% year-over-year, with growth across all channels and most end markets. South America core sales declined low to mid single digits.

On slide 8, we show the key components of our year-over-year change in adjusted earnings per share. Operating performance contributed approximately \$0.02 per share, driven by core growth and higher adjusted EBITDA margin. A lower tax rate contributed \$0.02 per share. Other items, including lower interest expense, lower share count and other income together generated about \$0.02 per share.

Slide 9 provides a summary of our cash flow performance and balance sheet metrics. Our free cash flow was \$73 million and represented 73% conversion to adjusted net income. Our restructuring cash outflows have increased, which impacted our free cash flow conversion. Our net leverage ratio declined to 2.0 times at the end of the third quarter, which was an improvement on a year-over-year and sequential basis.

During the quarter, we paid down \$100 million of gross debt. We expect our net leverage to be under 2 times at calendar year end 2025. Our trailing 12 month return on invested capital was 21.6%, an improvement sequentially, as improved operating performance helped offset the impact from internal investments in high return projects.

On slide 10, we provide our updated 2025 guidance. We have trimmed our core revenue growth midpoint to 1% and narrowed the range from 0.5% to 1.5% to reflect current macro conditions for the balance of the year. In addition, we have maintained our \$780 million adjusted EBITDA midpoint and narrowed the range to \$770 million to \$790 million.

We have raised our adjusted earnings per share guidance to the range of \$1.48 per share to \$1.52 per share, the upper half of our previous range. The \$1.50 per share midpoint reflects a \$0.02 per share increase relative to our prior guidance. Our guidance for capital expenditures is unchanged. We have lowered our free cash flow conversion outlook to a range of 80% to 90%, from 90% plus as a result of increased restructuring cash outlays as part of our footprint optimization and restructuring initiatives.

Turning to slide 11, we want to provide an update of our ongoing restructuring plans, as well as the strategic system conversion that we have been working on and that we expect to be complete by the middle of 2026.

Beginning right in Q4 2025 and finishing by the end of Q2 2026, we expect to close multiple factories, complete a labor realignment and go live with an ERP conversion for most of our European footprint. As we complete these activities, we will be focused on providing continuity and service for our customers and our affected team members. We expect to incur additional cost and other one-time operational impacts from these projects in the first half of 2026.

From a financial perspective, we anticipate an unfavorable year-over-year impact of 100 to 200 basis points to our adjusted EBITDA margin in the first quarter and a more modest unfavorable effect in the second quarter, ranging from 25 basis points to 75 basis points year-over-year.

In the second half of 2026, as we look towards completion of these various projects, we expect operations to normalize and realize favorable impact to our adjusted EBITDA margin from our restructuring activities of 75 to 125 basis points year-over-year. Excluding volume considerations, we expect our footprint optimization, restructuring and material cost out activities to generate 0 to 25 bps overall adjusted EBITDA margin improvement year-over-year for the full year 2026. We anticipate being at a 23.5% adjusted EBITDA run rate in the second half of 2026 in a volume neutral environment.

As I said, we have not taken volume impacts into this analysis and plan to update those assumptions as well as provide further insight into our restructuring activities when we initiate our formal 2026 guidance in conjunction with our Q4 earnings call in February.

I will now turn the call back over to Ivo.

Ivo Jurek

Chief Executive Officer & Director, Gates Industrial Corp. Plc

Thank you, Brooks. Moving to slide 12, this is our illustrative update on our walk towards the mid-term stated adjusted EBITDA margin target of 24.5%. In 2025, we have experienced a highly fluid business environment and continuation of prolonged negative PMI prints, resulting in constrained volume performance. With that as a backdrop, we now anticipate to complete our initial phase of the committed footprint optimization project by mid-2026 and still expect that those projects will achieve 100 basis points of savings from the footprint optimization program exiting 2026.

Coupled with our ongoing focus on material cost savings in 80/20, we estimate that our adjusted EBITDA margin will be nearing 24% on a run rate basis, exiting next year. Most importantly, this does not assume any margin benefit from a potential broad volume recovery in our industrial end markets. While the end market volatility has not been supportive, we are very pleased with our execution and performance to date. We believe the prospects for incremental improvement over the mid-term are positive, especially as the end market conditions begin to potentially inflect.

With that, let me summarize our views on slide 13. We believe we have executed well, delivering solid results given the lackluster demand environment we have encountered throughout this year. We generated record third quarter adjusted EBITDA margin rate and achieved our highest quarterly core growth rate since Q2 2023.

For the year, we are on target to deliver adjusted EBITDA margin expansion and earnings growth in a muted demand backdrop. We continue to make progress with our personal mobility and data center strategic initiatives and believe we will encounter a better industrial demand landscape in 2026.

We continue to adjust our structural cost base and we expect our savings to begin to compound during the second half of 2026 and anticipate our adjusted EBITDA margin rate to be approaching near 24% exiting next year. With that as a baseline level, we would expect any volume improvements to be additive to our margin performance.

Lastly, we believe we now possess a strong balance sheet that can be utilized to support various potentially value-creating capital deployment options. Our board recently approved a new \$300 million share repurchase authorization. Separately, debt reduction continues to be an option. We just repaid \$100 million of debt during the third quarter. And of course, at this juncture, our ability to execute bolt-on M&A transactions is increasing as we move towards our mid-term financial leverage target.

Before taking your questions, I want to thank the approximately 14,000 Global Gates Associates with their diligence and commitment supporting our customer needs. With that, I will now turn the call back over to the operator for Q&A.

QUESTION AND ANSWER SECTION

Operator: Thank you. We will now begin the question-and-answer session. [Operator Instructions] We do ask that you limit yourself to one question and one follow up. Your first question comes from the line of Nigel Coe with Wolfe Research. Please go ahead.

Nigel Coe

Analyst, Wolfe Research LLC

Q

Oh, thanks. Good morning, everyone. Thanks for the first question.

Ivo Jurek

Chief Executive Officer & Director, Gates Industrial Corp. Plc

A

Hi, Nigel.

Nigel Coe

Analyst, Wolfe Research LLC

Q

I just wanted to maybe clear up just some questions around slide 12. So it's very clear that the 24% for 2027 is to be viewed as more of a floor here, right. I mean, if we continue to just bump along the bottom here, 24% is where you see margins and then volume gives us some upside. I just want to make sure that that's the case. And then maybe just dig into some of these kind of costs you're flagging for the first half of the year and what sort of benefits you see from this ERP implementation?

Ivo Jurek

Chief Executive Officer & Director, Gates Industrial Corp. Plc

A

Yeah. Thanks, Nigel. Let me take the first part of your question and then I'll pass it off to Brooks on the ERP side and some of the other attributes of the cost question that you've had. But thinking about slide 12, right, so that

margin block was created, if you think about it more to provide you with an opportunity to model the impacts of the transitory costs to be incurred as a part of our restructuring program restart. And that the program is intended to significantly improve our cost structure all else equal, right, so not representative of growth forecast for our top line in 2026. So to your point, this is kind of a foundational floor.

We do expect growth in 2026. The margin impact for the full year in our presentation deck, however, excludes any benefit from revenue growth, frankly, because we are not providing you an updated guidance for 2026 yet. As you know, we will do that at the conclusion of our Q4 fiscal year and we'll do that in January.

So, look, we, we certainly believe that many of our end markets are at trough or close to troughing, as I said in my prepared remarks. And we believe that they will turn positive in 2026. In addition, we are excited and I said in a number of these calls over the last couple of quarters, we are quite excited about the strategic revenue generation initiatives for next year. And we certainly expect them to contribute nicely to our growth trajectory in 2026. With that, Brooks, if you want to take the second part of the question, please.

Lawrence Brooks Mallard

Executive Vice President & Chief Financial Officer, Gates Industrial Corp. Plc

A

Yeah. So there's several things that we expect from a one-time cost perspective relative to the restructuring and the head count alignment as we do the restructuring. There'll be, we expect, some additional freight cost, expediting costs, redundant labor costs and productivity cost as we move through some of these relocations. And that's normal course of business.

We do expect, to Ivo's point, I want to remind everyone, a lot of the backdrop for the reason we're doing a lot of these footprint optimization activities is to support our future growth. And so yes, we're going to get a cost benefit, but even more over we're going to have additional capacity both from machinery and equipment perspective, but more importantly, more capacity from a labor perspective to ramp through the cycle.

From an ERP perspective, we're replacing a fairly antiquated system with a new system that's going to provide us much more capability in terms of warehouse management, in terms of, managing the front the front end of the business to the back end of the business. But we really haven't built any of those benefits into our outlook. We've been very neutral on building those benefits in, but we definitely expect to improve our efficiencies and capabilities and again, support the strategic initiatives of the company with the ERP. But it does take – we do think it'll take us the first half of the year to get that all lined out, which is why we wanted to be transparent and provide you an update of the cost and the impact associated with those activities.

Nigel Coe

Analyst, Wolfe Research LLC

Q

Oh, yeah. We definitely appreciate that. Thank you. Just want to double click on growth. You mentioned growth about four or five times there. What kind of tailwinds or visibility do you have right now on some of the structural growth vectors like data center, personal mobility? I'm guessing you're going to have some price carry forward for next year. But more importantly, when you talk about the bottoming in some of these off-highway, on-highway markets, how much visibility do you have on production schedules for your OEM partners? And do you have any visibility on maybe kind of a turn in production for those end markets?

Ivo Jurek

Chief Executive Officer & Director, Gates Industrial Corp. Plc

A

Yeah, sure. So look, great question, Nigel. Thank you for asking that. Very, very optimistic, as you probably noticed over the last couple of earnings calls about some of the growth vectors, such as personal mobility and liquid cooling and data centers. The personal mobility, I think on the last call, we suggested that we anticipate kind of over the next three years and again, while that's not going to be every quarter, I want to remind everybody that things are not always linear. But it's going to take next three years, personal mobility.

We anticipated personal mobility to grow kind of 30% year on year compound annually between 2025 and 2028, right. And there'll be time that it's going to grow 22% to 25%. There'll be time, that it's going to grow 35%. But on aggregate, we believe that it's going to grow by 30% compound annually. And we have that confidence because of the design wins that we've been talking to you about over the last couple of years. The destock post-COVID has occurred and obviously we are delivering a real nice acceleration to the growth trajectory. And that will continue into the next couple of two years to three years. So we are quite positive about that.

We've talked about the accelerated adoption of liquid cooling. And while I'm not ready to give you a forward-looking revenue forecast for 2026 today, and I'll do more of that on our next call. We are seeing tremendous amount of activities out there. And there are some real positive attributes, because what we are realizing is there's more cooling that's required, not less, in the projects that we are involved with.

And we are seeing pretty substantial growth across the various customer base in the designing activity. And that's a really good precursor into what will be occurring for the next 12, 24, 36 months. So think about it kind of in a similar vein as when we were discussing personal mobility. So we believe that over the next one to two quarters, we're going to be giving you some more tangible attributes associated with the dollars and cents about what that's going to represent in 2026 and 2027. But so far, quite, quite optimistic about what we see there.

Our automotive replacement market, while we don't necessarily talk about it as a necessarily a growth [indiscernible] (00:32:38) we have been growing that market quite substantially and quite nicely over the last couple of years, provided a great deal of stability for our revenue generation. And we believe that that's going to continue as we move into 2026, 2027 and 2028. There's still plenty of opportunity, plenty of firepower left to be able to continue to grow that market in that kind of 2% to 3% range, which is about a nice for a more mature type level of applications. So put that aside from kind of the incremental over and above, if you would, growth trajectory to kind of your standard base.

Then when I take a look at some of our more traditional end markets, look, we certainly believe that the auto OE business, while it does not represent a significant size of our business. That's stabilizing and we believe that we will start seeing more additive growth rates in North America and ultimately in 2026 in Europe. So we believe that those markets are stabilizing. Post Liberation Day announcements that these companies are starting to – different countries are developing different agreements with administration. And I think things are starting to stabilize there. I think people are becoming little more optimistic about that end market.

We see some positive I would say formation of green shoots certainly in commercial construction end market. And we are starting to hear more positive news about what our customers expect there. Ag is still challenged and I talked about – ag actually got incrementally worse for us in Q3 while we have delivered maybe a positive core growth overall in ag. It got a little bit worse than what we've anticipated, but we do believe that that's troughing.

And that while it's not going to go off to the races in 2026, it's going to be significantly less bad than it has been over the last eight quarters. And so we are somewhat positive about that. And then ultimately, the diversified industrial market we've talked about it being kind of more kind of bottoming out over the last couple of quarters and we certainly believe that that's bottomed out and that should start being more accretive in 2026.

So I don't want to give anybody an idea that we have come out and we have given a forecast that we will not anticipate to have an organic growth rate in 2026. We are actually quite optimistic about it, but we just wanted to give you a visibility on modeling of certain structural cost removals that are going to be going in and out of the first half of the year and resetting our cost structure, becoming more competitive, and giving ourselves the opportunity to actually support that growth rate, which we are very optimistic about.

Nigel Coe

Analyst, Wolfe Research LLC

Q

Great, color. Thanks, Ivo.

Operator: Your next question comes from the line of Deane Dray with RBC Capital Markets. Please go ahead.

Deane Dray

Analyst, RBC Capital Markets LLC

Q

Thank you. Good morning, everyone.

Lawrence Brooks Mallard

Executive Vice President & Chief Financial Officer, Gates Industrial Corp. Plc

A

Hey, Deane.

Ivo Jurek

Chief Executive Officer & Director, Gates Industrial Corp. Plc

A

Good morning.

Deane Dray

Analyst, RBC Capital Markets LLC

Q

Hey. Wanted to circle back on slide 12 again. I know you've given this as a margin walk, and I don't know if you've provided this previously, but can you give us some dimensions of the restructuring like how many plants? Where are they? What kind of head count reduction, the dollar amount being invested and the dollar kind of payback cadence. I know you're providing it as a margin, but it would be helpful if you provide that dimension to it as well. Maybe you're restricted. I know that if it's outside the US, you've got some works council, but maybe if you could start there, that'd be helpful.

Lawrence Brooks Mallard

Executive Vice President & Chief Financial Officer, Gates Industrial Corp. Plc

A

Yeah. So look, Deane, it's fairly complicated because it's a combination of, if you remember when we said, we were doing the restructuring. It was mostly around North America and EMEA, right. So we'll kind of leave it at that we're closing multiple factories and there'll be hundreds of affected employees.

I would say the payback generally ranges from one to two years depending on the amount of severance, the amount of move, the amount of investment that we need to make. When we talk about the headwinds, just to kind of size it, we talked about 100 bps to 200 bps and 25 bps to 75 bps. That's kind of a \$30 million to \$35 million one-time expectation for the first half of 2026. And that it also includes the system conversion and all the costs associated with that.

And so from a – I would say the other part, if you think about our increased capital spend over the past couple of years that's part of the investment as well, right. And so if you look at what we spent over the past couple of years, you could say maybe \$20 million last year, \$20 million this year. So that's part of the investment as well.

So when you calculate all that up that gives you that one to two year payback, again, depending on the timing of when the projects get implemented and when the savings come through. And as I said, we feel as we exit the second half of 2026, the first part of all that restructuring will be complete and you'll see the flow through in the second half.

But let me also say that we're still working on additional projects and there's still money that we're spending right now that's kind of part of that group the investment I talked about that we haven't put into our run rate yet, that we haven't disclosed yet, right. Because when you think about the back half of the year there's probably \$5 million per quarter, so \$10 million in the back half of the year of savings, which will also roll over into the first half of 2027. So that's kind of \$20 million or half of the \$40 million. So we're still working on the other half and those projects will be implemented and we'll disclose those here over the next year or so. Hopefully that kind of gives you enough color in terms of how all those things are working.

Deane Dray

Analyst, RBC Capital Markets LLC

Q

Yes, it really did. I appreciate that additional color. And then as a follow-up, I was hoping you could take us through kind of the tariff impact pricing. And do you see any, and it sounds like there could be some volume falloff because of some demand destruction, but just kind of where does tariff stand on a net basis?

Lawrence Brooks Mallard

Executive Vice President & Chief Financial Officer, Gates Industrial Corp. Plc

A

So let me take the cost piece and I'll let Ivo talk about the volume piece. So from a cost basis, we're okay in terms of the total EBITDA impact. What I would say, though, as you look at some of the gross margin dilution in the back half of 2025 and that will fall through to EBITDA dilution. We're probably seeing 30 bps to 40 bps of dilution because we're not, we're not getting anything in terms of bottom line add from the tariffs, right. We're just kind of holding our own and making sure that we don't cost ourselves money. So the impact from a profitability perspective is kind of 30 bps to 40 bps, \$0 from a from a total EBITDA dollars perspective. And then I'll pass it over to Ivo to talk about the volume.

Ivo Jurek

Chief Executive Officer & Director, Gates Industrial Corp. Plc

A

Yeah, Deane. I think that I am not sure whether I would call it volume destruction or what have you, but I think I would say call it more of a short term transitory growing pains. I believe that there's probably some impact to Ag, in particular. Certainly the trade environment has gotten more challenging, particularly for farmers. And that's kind of what we have seen in terms of probably delayed recovery in ag overall.

And as I said on the call ag in Q3 got slightly worse than what we've anticipated at the beginning of Q3 around the edges, but we do believe that that market will also start normalizing as we as we enter 2026 and sometimes during 2026 it should start getting little less negative.

So, around that, I think that you're starting to see more stabilization around the auto businesses. Overall, I think you start seeing forecasts maybe getting a little more positive in terms of production output by the carmakers. So I

think that some of those transitory headwinds are probably abating and as we enter 2026, I think the environment should be more stable.

Deane Dray

Analyst, RBC Capital Markets LLC

Thank you.

Q

Lawrence Brooks Mallard

Executive Vice President & Chief Financial Officer, Gates Industrial Corp. Plc

Thanks, Deane.

A

Operator: Your next question comes from the line of Julian Mitchell with Barclays. Please go ahead.

Julian Mitchell

Analyst, Barclays Capital, Inc.

Hi. Good afternoon. Maybe just the first question, I'm trying to drill into perhaps a little bit the sort of exit rate from 2025. Just looking at the fourth quarter, for example, you mentioned Ivo, the sort of firming of the industrial environment in the prepared material, but I think the revenue guide seems to embed sort of fairly normal seasonality for the fourth quarter. Just wondered if you could clarify that? And then similarly on kind of the EBITDA rate in the fourth quarter, often down sequentially. I think this time it's sort of flat to up. Just wondered if there was anything to call out there in terms of enterprise initiative benefits or mix or something?

Q

Ivo Jurek

Chief Executive Officer & Director, Gates Industrial Corp. Plc

Yes. So look, Julian, I think that you said it correctly. I mean, if you think about our Q4 revenue, it really is kind of taking exit rate, Q3 environment, applying normalized seasonality. So there really isn't anything peculiar. I wouldn't say that we have baked in any further recoveries. We obviously are very cautious around ag, but we're taking that present environment and we say you're probably not going to really see any tangible change in Q4.

A

And take into account that many of these end markets, many of our customers have had somewhat challenging years, so I don't see anybody trying to pre-position themselves for 2026. And that, in a way, I would say is positive that folks are not prepositioning themselves. I think that people are now focusing more on 2026. And we are seeing or we are hearing certainly more kind of an optimistic outlook, about 2026 in certain segments of our business. So, that being said, on the demand. And I'll let Brooks chime in on the EBITDA for Q4.

Lawrence Brooks Mallard

Executive Vice President & Chief Financial Officer, Gates Industrial Corp. Plc

Yeah. So from a Q4 perspective we're still seeing some – we're seeing some of our initiatives roll through around material cost. Sort of that's offset by some of the tariff dilution. And we've got normal seasonality in terms of Q4. I think we're pretty happy with where our inventories are in terms of service and in building being ready for some of these activities in Q1. So we're not building significant inventories as we head into the end of the year. So all in, nothing – some puts and takes, right, in terms of things working in our favor. Other things that we're taking on and making sure that we're able to deliver EBITDA growth year-over-year, but nothing structurally different as we end the year.

A

Ivo Jurek

Chief Executive Officer & Director, Gates Industrial Corp. Plc

A

And Julian, we also execute – we are also executing rather well, right. I mean, we have 18% EPS growth in Q3, record level of margins, in a reasonably muted end market environment. So I think that the organization is doing a good job in managing during some of these challenging times and frankly, delivering differentiated operating results.

Julian Mitchell

Analyst, Barclays Capital, Inc.

Q

Great. And then just one quick follow-up on the sort of cash conversion. I think you walked down the guide a bit there. There's some higher cash restructuring. Should we expect much improvement in conversion next year or no, because of the EMEA and North America restructuring charges will sort of lay on next year.?

Lawrence Brooks Mallard

Executive Vice President & Chief Financial Officer, Gates Industrial Corp. Plc

A

Yeah, we'll have to take a look at that. I mean, I would think that the bigger part of what's affecting us in 2025 is the restructuring charges that are an add back to adjusted EBITDA and adjusted net income, but flow through the free cash flow and then the higher CapEx as well.

I would say that we're going to continue to spend CapEx, although I would imagine it starts to dial down just a tad in 2026. And we will probably see some small headwinds related to the restructuring, cash out versus how it shows up in adjusted net income, but probably not as much as we do this year.

And, again, we called out the headwinds. Those are going to show up in the numbers and show up in the cash. And so that won't really affect the overall cash conversion number because those will be in both places. So we'll update that and we'll make sure that we call that out specifically when we update our guidance for 2026, but again, that's really just a kind of it's in one number. It's not in the other number. And so it's a little bit out of balance. We need to make sure we call that out in our cash conversion.

Julian Mitchell

Analyst, Barclays Capital, Inc.

Q

Great. Thank you.

Operator: Your next question comes from the line of Jeff Hammond with KeyBanc Capital Markets. Please go ahead.

Jeffrey D. Hammond

Analyst, KeyBanc Capital Markets, Inc.

Q

Hey, good afternoon. Appreciate all the color. So just to kind of put a bow on this noise around margins and the margin bridge because I think the message is getting confused that next year is a transition year and maybe your long-term targets getting pushed out. It seems like to me you had said to get to your margin target, you needed 100 to 150 basis points from volume. And that hasn't played out. And it seems like you've maybe outperformed on internal execution, material savings and the volume has been the whole, but maybe just level set me on that.

Ivo Jurek

Chief Executive Officer & Director, Gates Industrial Corp. Plc

A

I think, Jeff, you just said it perfectly. We're actually delivering on our mid-term targets without getting any help from the underlying macro. And we feel really good about that, right, because it's really tough to execute in such negative PMI environment. And so I think that there was the point of delineation where we want to ensure that we communicate to the markets that the company is executing well.

We certainly believe that the volume is going to inflect. We all certainly know that none of us are very good at being able to call the inflections in the macroeconomics, taking into account that there are so many different moving pieces associated with trade policies and industrial policies and kind of the global behavior of these end markets itself. But I think all of us would anticipate it after 36 months of negative PMI, we would be on a verge and at some point in time to see some inversion. And when that occurs, obviously, that's incremental to what we have described in our presentation.

Jeffrey D. Hammond

Analyst, KeyBanc Capital Markets, Inc.

Q

Okay, great. And then just on capital allocation, I sense a little bit of a tone change where you kind of been saying before, hey, we're just going to buy back our stock. The market doesn't appreciate what we're doing here. And the multiple hasn't expanded relative to our peers, but now it seems like you're maybe talking a little more about bolt-ons. And so am I reading that right or do we lean in on a day where stock's down 6% and the market's confused?

Ivo Jurek

Chief Executive Officer & Director, Gates Industrial Corp. Plc

A

Yeah, look, I mean, I think our stock is inexpensive. It's trading at a valuation that is not akin to the performance that the company is delivering. So we'll certainly lean into buybacks. The board authorized \$300 million of buyback. So we'll certainly be utilizing what we can. But the company as well is generating tremendous amount of free cash flow. So I think that we can do all of the things that have that have been outlined as plausible outcomes for capital deployment.

We've bought back – I mean, we've paid down some more debt. We will be strategic about buying back our stock, but we also believe that as our balance sheet is trending towards below the 2 times leverage that we have kind of put in in the places of demarcation point for us. And so hopefully I won't have to be talking about leverage in the future. We believe that we can use all three levers for capital deployment. And we will be leaning more aggressively towards bolt-on M&A.

Jeffrey D. Hammond

Analyst, KeyBanc Capital Markets, Inc.

Q

Great. Thanks, guys.

Lawrence Brooks Mallard

Executive Vice President & Chief Financial Officer, Gates Industrial Corp. Plc

A

Thanks, Jeff.

Operator: Your next question comes from the line of Andy Kaplowitz with Citigroup. Please go ahead.

Andrew Kaplowitz

Analyst, Citigroup Global Markets, Inc.

Q

Hey, good morning, everyone, or good afternoon now.

Ivo Jurek

Chief Executive Officer & Director, Gates Industrial Corp. Plc

Hi, Andy.

A

Lawrence Brooks Mallard

Executive Vice President & Chief Financial Officer, Gates Industrial Corp. Plc

Hi, Andy.

A

Andrew Kaplowitz

Analyst, Citigroup Global Markets, Inc.

Ivo, you've been talking about accelerating footprint optimization and doing 80/20 since your Investor Day a year-and-a-half ago, but obviously, your growth since then has been somewhat slow. So I'm just trying to figure out if you're accelerating or enhancing any of your restructuring plans versus when you updated us at that Investor Day. And then maybe can you update us on how 80/20 is impacting Gates as you go into 2026 and beyond? If you do organically grow, can you do core incrementals over 40%?

Q

Ivo Jurek

Chief Executive Officer & Director, Gates Industrial Corp. Plc

Yeah, look, I think that I want to kind of be fully transparent, right. So as the Liberation Day came forward in April, we kind of took a little pause to try to understand what will the new mercantile regime look like and how do we how do we think about our overall operating structure as a company. And obviously, we have been [indiscernible] (00:53:20) for a long time. So we just wanted to reassess and get a better sense of what is happening in the world.

A

I think that as we got more comfortable with what we are seeing and how we are organized, we've come to the conclusion that our original plan was the right plan. As Brooks indicated, we need to be capable of having an access to labor that will give us an ability to flex up and down as these cycles occur. We believe that we are on the verge of an upcycle, so we've got to be positioned well to support the growth that we anticipate over the next upcoming upcycle.

And so we are really just executing on our original plan, Andy. Nothing really has dramatically changed around what we have anticipated vis-à-vis our footprint optimization and restructuring. So I think we are in a very, very good shape. And it also validated our plan, was the right plan. We just needed to hit a pause for a couple of quarters. So that that's kind of beyond us and we are moving forward.

As to 80/20, look, 80/20 material cost reductions and driving a better operational focus have been really the attributes that have given us the opportunity to outperform what we have anticipated during our Capital Markets Day in 2023 and still deliver on our mid-term targets without the growth. So it's a very powerful tool. We, again, believe that we are in the very early innings. We take a look at somebody like ITW that has been doing it for over a decade plus and they continue to deliver good margin expansion.

We believe that we not only have the opportunity for a very certainly in immediate future to continue to support 80/20 as a key attributes of our enterprise initiatives, to add to our profitability, but also grow our franchise through our strategic growth verticals. So we think that we can do both, and we think that 80/20 is going to be very additive to us.

And if you exclude the benefits from restructuring and again, I want to be very specific if you exclude the benefits that we have described on slide 12, we still believe that in a normalized growth environment that we anticipate kind of in 2026 and beyond, we should be generating 30% to 35% incremental over and above the benefits that I described on that page.

Andrew Kaplowitz

Analyst, Citigroup Global Markets, Inc.

Q

Ivo, that's helpful. And then just in terms of growth by region, I think you explained what's going on in North America well, but you also mentioned EMEA returned to growth, which is interesting. And China continues to put up durable growth for you guys. So maybe you could sort of click on or give us little more color about what you're seeing?

Ivo Jurek

Chief Executive Officer & Director, Gates Industrial Corp. Plc

A

Yeah, look, I mean, I think that North America has been probably most challenged from kind of agriculture end market exposure that got slightly worse. And I remember, it wasn't a ton of dollars that it got around the edges, less supportive than what we have anticipated. So it's just around the edges, less supportive there.

The other end markets, look, I mean, automotive overall grew nicely. Automotive replacement grew really well for us in North America. Our industrial replacement market is growing. So the things they're not bad in any form of imagination. They're kind of around what we have anticipated, maybe slightly worse behavior in the ag environment.

South America has been tough last quarter, but it's been predominantly tough after extraordinary several quarters or maybe six quarters of significant growth. So it's kind of a more normalization and we, again, anticipated South America is going to start moving into the growth phase as we kind of exit 2025 into 2026.

Europe, I mean, Europe has been a little bit surprising to us, right, I mean, behave a little bit better than what we've kind of envisaged with positive core growth. I would say that the auto markets are quite negative in Europe. I don't think I'm telling you anything that that has not been already communicated, but our AR business is performing well. Our Industrial First Fit, particularly around the commercial construction segment and mobility, has been performing quite well. And IR has been stabilizing and starting to perk up a little bit in in Q3. So maybe around the edges, more green shoots than less.

And China, China has been okay. Automotive has been doing quite all right for us in China, industrial replacement has been doing quite all right for us. So China has been behaving more or less as we have seen over the last several quarters.

And the East Asia and India is growing. I mean, we are growing nicely automotive replacement business in India. The Industrial First Fit business is doing well. I mean, I think that India is poised to continue to be on a trajectory of nice growth with the overall economy evolving nicely and becoming a real alternative to China over the mid-term. So we are quite optimistic about what we can see out of India in particular. So overall, we actually are reasonably tending to be more optimistic than less. And we believe that 2026 should be more positive than perhaps might have been taken out of our release today.

Andrew Kaplowitz

Analyst, Citigroup Global Markets, Inc.

Q

Thanks for all the color.

Operator: Your next question comes from the line of Tomo Sano with JPMorgan. Please go ahead.

Tomohiko Sano

Analyst, JPMorgan Securities Japan Co. Ltd.

Hello, everyone.

Q

Ivo Jurek

Chief Executive Officer & Director, Gates Industrial Corp. Plc

Hi, Tomo.

A

Lawrence Brooks Mallard

Executive Vice President & Chief Financial Officer, Gates Industrial Corp. Plc

Good morning.

A

Tomohiko Sano

Analyst, JPMorgan Securities Japan Co. Ltd.

Hi. I'd like to ask about the data centers and of the \$322 million in fluid power revenue this quarter, how much was it related to data center sales? And what is your expectations for 2025 data center revenue and the conversions of your \$150 million plus pipeline in 2026 please?

Q

Ivo Jurek

Chief Executive Officer & Director, Gates Industrial Corp. Plc

Yeah. Tomo, good afternoon to you. Good morning. We are not going to be addressing exactly the revenue flows because it's still reasonably a small size of revenue that is growing rather nicely for us, but from a very, very small base, so I don't think it's worth, at this point in time, to spend time yet on the sizing of this. It's still in millions, not in the tens of millions yet.

A

Design-in activity remains very, very robust. I mean, we see significant number of new customers that that are coming to us. And we are working with on new design-in opportunities. And we will be providing you with some additional color in January, or early February on our Q4 earnings call. But we do continue to be quite optimistic that the data center growth and as a vertical is going to ramp up rather nicely. And we still feel that that \$80 million to \$200 million, \$100 million to \$200 million by 2028 is certainly doable for us as an intermediate target for us over the next two to three years. We also, incidentally, are going to be at the show, Super Compute next, I think a few weeks from now in St Louis. So we would invite anybody to stop by and have a conversation with us about some of the new products innovation. We can provide additional color on what we are working on from a technology perspective there as well.

Tomohiko Sano

Analyst, JPMorgan Securities Japan Co. Ltd.

Thank you, Ivo. And a follow up on pricing perspective. Could you talk about how effective you have been in passing through cost inflation in Q3? And what is your pricing strategy for 2026, please?

Q

Lawrence Brooks Mallard

Executive Vice President & Chief Financial Officer, Gates Industrial Corp. Plc

A

Yeah, well, I mean, going back, I mean, we've always been, I would say, as effective as anybody in terms of passing pricing through from an inflation perspective, when all the new tariffs came out, for the most part, we're able to cover that with pricing. I mean, there are certain regions where that are a little bit more pricing challenged. Particularly in Asia, where we were able to it more operationally than through pricing. We've always been very transparent in terms of we're going to cover material utility inflation on a yearly basis with pricing.

And then the 80/20, when we implemented 80/20 we added a value pricing lever to our pricing tactical approach. We make hundreds of thousands of SKUs, right. And so some of these SKUs you want to be more competitive on. Some of them, we're the only ones that make it. And you can price those based on the value you bring, because you may be the only one that makes that particular part. And so we continue to use our 80/20 playbook to optimize pricing. And in the aggregate we're always going to make sure that we use pricing to cover our material and utility inflation.

Tomohiko Sano

Analyst, JPMorgan Securities Japan Co. Ltd.



Thank you. Appreciate it.

Operator: That concludes our question-and-answer session. I will now turn the conference back over to Rich for closing comments.

Rich Kwass

Vice President, Investor Relations and Strategy, Gates Industrial Corp. Plc

All right, thanks, everyone, for joining. If you have any further questions, feel free to reach out. Otherwise, have a great rest of the week. Take care.

Operator: Ladies and gentlemen, this does conclude today's conference call. Thank you for your participation and you may now disconnect.

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