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APi Group Corp. (APG)

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MANAGEMENT DISCUSSION SECTION

Operator: [Operator Instructions] Good morning, ladies and gentlemen, and welcome to APi Group's Third Quarter 2023 Financial Results Conference Call. All participants are now in a listen-only mode until the question-and-answer session. Please note, this call is being recorded. I will be standing by should you need any assistance.

I will now turn the call over to Adam Fee, Vice President of Investor Relations at APi Group. Please go ahead.

Adam Fee

Vice President-Investor Relations, APi Group Corp.

Thank you. Good morning, everyone, and thank you for joining our third quarter 2023 earnings conference call. Joining me on the call today are Russ Becker, our President and CEO; Kevin Krumm, our Executive Vice President and Chief Financial Officer; and Sir Martin Franklin and Jim Lillie, our Board Co-Chairs.

Before we begin, I would like to remind you that certain statements in the company's earnings press release announcement and on this call are forward-looking statements, which are based on expectations, intentions and projections regarding the company's future performance, anticipated events or trends and other matters that are not historical facts. These statements are not a guarantee of future performance and are subject to known and unknown risks, uncertainties and other factors that could cause actual results to differ materially from those expressed or implied by such forward-looking statements.

In our press release and filings with the SEC, we detail material risks that may cause our future results to differ from our expectations. Our statements are as of today, November 2, and we undertake no obligation to update any forward-looking statements we may make except as required by law. As a reminder, we have posted a

presentation detailing our third quarter financial performance on the Investor Relations page of our website. Our comments today will also include non-GAAP financial measures and other key operating metrics. The reconciliation of and other information regarding these items can be found in our press release and our presentation.

It is now my pleasure to turn the call over to Jim.

James E. Lillie

Co-Chair, APi Group Corp.

Thanks, Adam. APi delivered another strong quarter of results, including record third quarter net revenues, adjusted EBITDA and adjusted diluted earnings per share in an evolving macro and foreign exchange environment. During our Investor Day last year, Russ detailed our strategy of focusing on growing our service-based recurring revenue, while slowing revenue growth in select businesses through improved project selection. Our goal of evolving away from lower-margin, higher-risk opportunities, while focusing investments on service revenue expansion is yielding the desired results. This strategy improves margins while simultaneously reducing capital spending, which in turn drives free cash flow generation.

The benefits of these initiatives is shown in APi's consistently strong and improving financial results. These results are built on strong foundation of driving the company's recurring revenue services-focused business model, while expanding the financial discipline of the organization and its leadership team. The team's relentless efforts on adhering to our strategy are driving margin expansion, and we believe there is a long runway of continued margin expansion beyond our established 2025 targets. As we look forward, we believe our balance sheet is even stronger following our repricing and maturity extension, and we expect to end the year below our targeted net leverage ratio of 2.5x.

Since becoming a public company, the team has enhanced their position as the number one provider globally in the growing, highly fragmented fire and life safety services market. Going forward, we are excited to build on our track record of disciplined, predictable and thoughtful decisions regarding capital allocation, with a primary focus on tuck-in M&A at accretive multiples. We have great confidence in the business, and we believe that our laser focus on our long-term 13/60/80 value creation targets will generate continued exceptional performance through 2025 and beyond.

As a reminder, our financial goals include long-term organic revenue growth above the industry average; adjusted EBITDA margin of 13% or more in 2025; long-term revenues of 60% from inspection, servicing and monitoring; and long-term adjusted free cash flow conversion of 80%. We look forward to continue to update you on our positive momentum on margin expansion, service revenue growth, the opportunities for solid organic growth in 2024 and beyond, our visibility on bolt-on M&A at accretive multiples and our strong balance sheet.

With that, I'm pleased to turn the call over to Russ for further details.

Russell A. Becker

President, Chief Executive Officer & Director, APi Group Corp.

Thank you, Jim. Good morning, everyone. Thank you for taking the time to join our call this morning. We truly remain grateful for the hard work of our 29,000 leaders and their dedication to APi. The safety, health and well-being of each of our teammates is our number one value. We will continue to invest in the men and women in the field as human beings and provide each of them with training, leadership development and advancement opportunities, because APi only wins when our branches and field leaders win.

Before getting into our results and our outlook, I wanted to share our thoughts and support for our leaders in Lewiston, Maine, who were tragically impacted by the horrific shootings there last week. Thankfully, three of our APi teammates who were present at the bowling alley were not harmed. As I said, the health and safety of our team is our number one priority, and this obviously extends beyond their work life and into their personal lives as well.

Jim mentioned our 13/60/80 long-term shareholder value creation model that you see once again included in our presentation. As I continue to detail on our quarterly calls and at events, investor conferences, we are consistently focused on driving this strategy, with a specific focus of achieving 13% adjusted EBITDA margins in 2025, while expanding the service, recurring revenue mix of the business.

The team has made strong progress this year, executing on our margin expansion initiatives, which has been accomplished by focusing on the following items: Pricing; improved inspection, service and monitoring revenue mix; disciplined customer and project selection; Chubb value capture; procurement systems and scale; accretive M&A as well as selected business pruning; and as I like to say, we can always just be better. We continue to see runway from these initiatives through 13% in 2025 and beyond.

Turning to the quarter, I'm again pleased with the record results delivered by our global team as we continue to see solid demand for the services we offer. And this is key. We are focused on picking the right opportunities to deploy our field leaders on the highest margin work. Net revenues grew organically by 1.3% in the quarter and by approximately 7% year-to-date, reaching \$1.8 billion for the three months ended September 30, 2023.

This lower organic growth in the quarter was primarily driven by our strategic focus and disciplined customer and project selection across the business, which drives improvement in margins and free cash flow conversion. In the quarter, organic growth in our services business remained strong at 7%, while our projects business contracted, as expected, by approximately 4%, as we continue to focus on disciplined customer and project selection to drive gross margin expansion.

US Life Safety once again posted solid organic growth of approximately 5% in the quarter after tough comp of 20%-plus organic growth in Q3 2022. This growth was led by consistent double-digit-plus core inspection growth, which we had achieved in our US Life Safety business each quarter since the start of the pandemic. Importantly, our service revenue grew organically by approximately 8% in the quarter, which both expands margins and strengthens the protected moat around the business. The strength in inspection growth and the subsequent service work pull-through continues to drive outsized growth in our higher margin inspection, services and monitoring revenues when compared to our project revenues.

On the projects side, end markets still matter, and we are focused on choosing the right ones. We see continued momentum in data centers, semiconductor, electric vehicle manufacturing, health care and critical infrastructure, with manufacturing and data center construction expected to increase by double-digits in 2024 depending on what source you're looking at. Our backlog remains healthy and continues to grow in the areas we are not intentionally pruning. All of this gives us confidence we can continue to grow our projects business organically in a margin-enhancing way, while still maintaining a focus on doing the right projects for the right customers in the right end markets.

In line with our strategic initiatives, we continue to see strong year-over-year improvements in adjusted gross margin in the third quarter, up 270 basis points. I am pleased with the leadership team's ongoing commitment to driving gross margin improvements through pricing activities, growing higher margin service work and maintaining

discipline in customer, project and end market selection. The strong performance in gross margin led to third quarter adjusted EBITDA margin of 12.6%, representing margin expansion of 190 basis points.

I'd like to take a minute to express my appreciation to all of our union partnerships. APi is a partner to over 200 smaller local unions, geographically spread across North America. These 200-plus relationships create a stable pipeline of highly-skilled technicians as well as a high level of diversification. As the leading employer for many of these unions, we truly appreciate the opportunity to provide highly-skilled field leader a career path at APi. Labor is our largest variable cost and the labor rate visibility our union relationships provide allows APi to drive margin expansion through its pricing activities. Our relationships with our unions is very healthy, with fair, long-term agreements in place that don't challenge our business the way the automotive industry has experienced.

The international business continues to show progress with another quarter of organic growth. The business has delivered organic growth six straight quarters since our ownership despite the transformation underway from a culture, go-to-market and branch-led operational perspective. Our leadership team in the international business continues to drive positive change and has done a great job with their focus on increasing profitability through driving price and by being intentional about targeting work that is additive to achieving our 2025 13% adjusted EBITDA margin target.

The opportunity in our international business continues to be substantial, and we are in the early innings of harnessing it. The brand equity, capabilities and technology in this business are differentiated, and we are actively addressing the operational efficiency of the organization through our \$100 million value capture plan, which remains on track. I expect that we will provide a more detailed update on our integration progress in the fourth quarter.

Moving on to M&A. As you have seen, we have returned to accretive bolt-on M&A with five closed transactions in our Safety Services segment this year, while delivering on our deleveraging commitment. Our leadership team has a long and successful track record of integrating businesses from both a cultural and operational standpoint, and our pipeline of opportunities in line with what we consider to be appropriate multiples is solid.

Looking forward, we'll remain active buyers of businesses with the right culture, values and strategic fit at the right multiples with a near-term focus on US life safety bolt-on acquisitions. The team continues their hard work prioritizing the most attractive opportunities in our robust M&A pipeline, and I remain excited to continue to add new businesses and their leaders to the APi family.

We also continue to review our existing businesses where needed to evolve APi into an even lower-CapEx asset-light business, focused on high-margin, statutorily-mandated services, with an emphasis on our 13/60/80 value creation targets. We don't spend much time talking about our ongoing reduction in capital spending as we shift the mix of the business, but to illustrate the improvement over the last five years, which we expect to continue, there is a new slide in our earnings presentation.

Additionally, we continue the intentional pruning of certain customers and loss-making contracts, primarily in our Specialty Services, HVAC and international businesses. This strategy has been a key driver of gross margin expansion, while also being a drag on reported organic growth. Looking ahead to 2024 and 2025, we have a solid backlog with incremental opportunities for growth at appropriate margins in the right end markets.

Occasionally, the pruning necessary to achieve our long-term financial goals will also include operating businesses or branches. Near the end of the quarter, APi reached an agreement to sell a traditional design-bid-build heavy civil contracting company without complementary service opportunity, which we felt was not

consistent with our long-term targets. This business delivered \$52 million of revenue to APi in the first nine months of 2023.

In summary, while we remain focused on executing in Q4 and into 2024, I am proud of our team and the record financial results achieved so far in 2023. Our field leaders continued to be the driving force of our performance. I'm grateful for what each of them has done to get us to where we are today.

I would now like to hand the call over to Kevin to discuss our financial results and guidance in more detail. Kevin?

Kevin S. Krumm

Executive Vice President & Chief Financial Officer, APi Group Corp.

Thanks, Russ. And good morning, everyone. Reported revenues for the three months ended September 30, 2023 increased by 2.8% to \$1.8 billion compared to \$1.7 billion in the prior year period, driven by strong services revenue organic growth of 7% and modest benefits from favorable foreign currency exchange rates and M&A. This was partially offset by our continued disciplined customer and project selection, lower material costs and customer project delays in Specialty Services leading to a 4% decline in our projects businesses versus the prior year. On an organic basis, revenues increased by 1.3%, off of 2022 comp of approximately 16% organic growth.

Adjusted gross margin for the three months ended September 30, 2023 grew to 29%, representing a record gross margin and a 270 basis point increase compared to the prior year period, driven by continued price increases, outsized growth in our higher margin services revenue as well as margin expansion for both our projects and services businesses across both segments.

Adjusted EBITDA increased by 19.1% on a fixed currency basis for the three months ended September 30, 2023, with adjusted EBITDA margin coming in at 12.6%, representing a 190 basis point increase compared to the prior year period, primarily due to the factors impacting gross margin. This was partially offset by investments to support ongoing revenue growth and the continued investment in building our global capabilities and infrastructure.

I'm pleased to report that adjusted diluted earnings per share for the second quarter was \$0.48, representing \$0.11 or 30% increase compared to the prior year period. The increase was driven primarily by strong continued margin expansion in both Safety and Specialty Services, partially offset by an increase in interest expense, representing a \$0.01 headwind to adjusted diluted earnings per share in the quarter.

I will now discuss our results in more detail for Safety Services. Safety Services reported revenues for the three months ended September 30, 2023 increased by 5.5% to \$1.217 billion compared to \$1.154 billion in the prior year period, driven by double-digit core inspection revenue growth, 8% organic growth in inspection, service and monitoring in the US Life Safety segment, as well as modest benefits from favorable foreign currency exchange rates and M&A. This was partially offset by flat growth in the projects business, driven by planned customer attrition in our international businesses, lower material costs and continued discipline in customer and project selection in our HVAC businesses. On an organic basis, Safety Services revenues increased by 3% off a 2022 comp of approximately 20% organic growth.

Adjusted gross margin for the three months ended September 30, 2023 was 33.3%, representing a record high adjusted gross margin and a 260 basis point increase compared to prior year adjusted gross margin, driven by continued price increases, improved business mix in inspection, service and monitoring revenue, as well as expansion in both our projects and services businesses. Adjusted EBITDA increased by 19.9% on a fixed currency basis for the three months ended September 30, 2023. and adjusted EBITDA margin was 13.9%,

representing a 190 basis point increase compared to the prior year period, primarily due to the factors impacting adjusted gross margin, partially offset by investments made to support ongoing revenue growth.

I will now discuss our results in more detail for our Specialty Services segment. In line with our plan to improve customer and project selection, Specialty Services reported revenues for the three months ended September 30, 2023 declined by 3.6% to \$565 million (sic) [\$569 million] (00:20:11) compared to \$590 million in the prior year period, driven by a 14% decline in project revenues due to the aforementioned continued disciplined customer and project selection, [ph] lower material costs (00:20:25) and customer project delays primarily in the fabrication business. This is partially offset by a 10% growth in our service revenues.

Adjusted gross margin for the three months ended September 30, 2023 was 19.7%, representing a 220 basis point increase compared to the prior year period, driven primarily by disciplined customer and project selection driving margin expansion in both our projects and services business. Adjusted EBITDA increased by 12.2% for the three months ended September 30, 2023. And adjusted EBITDA margin was 14.6%, representing a 210 basis point increase compared to the prior year period, primarily due to the factors impacting adjusted gross margin.

We continue to focus on driving free cash flow conversion improvements year-over-year, progressing towards our 2023 target of 65%-plus adjusted free cash flow conversion. For the three months ended September 30, 2023, adjusted free cash flow came in at \$146 million, reflecting an adjusted free cash flow conversion of 65%. For the first nine months of the year, adjusted free cash flow was \$237 million, with conversion of 41%, representing an improvement of \$55 million or 30% when compared to the first nine months of 2022.

Free cash flow generation has been and continues to be a priority across APi, and our performance in the first nine months of the year puts us in a position to achieve our 2023 guidance at or above 65% adjusted free cash flow conversion as we head into the fourth quarter which due to seasonality is traditionally our strongest free cash flow conversion quarter.

On October 11, we closed the successful repricing of our term loans due 2026 and 2029, achieving a 25 basis point reduction in our borrowing rate with no change to our covenants, representing approximately \$4 million of annual cash interest savings, all while extending our weighted average maturity. As part of the transaction, APi repaid \$100 million of the term loan due 2026 and moved over \$400 million of it to the term loan due 2029.

We expect to pay down an additional \$150 million of the term loan due 2026 in the fourth quarter, totaling approximately \$450 million for the full year, further reducing cash interest expense on a go-forward basis. At the end of the year, we expect to have \$355 million remaining on the term loan due 2026.

At the end of the third quarter, our net debt to adjusted EBITDA was approximately 2.7 times. Even as we return to margin-accretive both on M&A, we remain laser-focused on cash generation and deleveraging below our stated long-term target of 2.5 times by year-end 2023. As we look forward to 2024, we expect to grow our adjusted free cash flow as well as improve our cash flow conversion, providing a significant opportunity for value-enhancing capital deployment.

I will now discuss our Q4 and full year 2023 guidance. As a reminder, our guidance is based on foreign exchange rates in effect at the time we report our quarterly results. During the third quarter, the dollar strengthened significantly, diminishing the expected year-over-year tailwind from changes in foreign currency exchange rates in the second half of 2023. The difference between actual and forecast rates impacted reported sales by approximately \$20 million in the third quarter. Based on current exchange rates, we now expect full year reported

net revenues of \$6.9 billion to \$6.95 billion, down from \$7.015 billion to \$7.075 billion. This represents organic net revenue growth of approximately 5% to 6%.

We are very pleased with the margin performance year-to-date, which gives us confidence to raise the bottom end of our prior full year guidance for adjusted EBITDA despite the foreign currency headwinds we saw during the quarter. We now expect full year adjusted EBITDA of \$775 million to \$785 million, up from \$765 million to \$785 million, which represents adjusted EBITDA growth of approximately 15% to 16% on a fixed currency basis and adjusted EBITDA margin of approximately 11.3% at the midpoint.

In terms of the fourth quarter, we expect reported net revenues of \$1.73 billion to \$1.78 billion. This guidance represents organic net revenue growth of approximately 1% to 4%. We expect fourth quarter adjusted EBITDA of \$200 million to \$210 million, which represent adjusted EBITDA growth of approximately 8% to 13% on a fixed currency basis.

For 2023, we anticipate interest expense to be approximately \$147 million, based on fourth quarter interest expense of approximately \$35 million; depreciation to be approximately \$80 million; capital expenditures to be approximately \$90 million; and our adjusted effective cash tax rate to be approximately 23%, down from 24%. We expect our adjusted diluted weighted average share count for the fourth quarter to be approximately 273 million shares.

As we look forward to 2024, where our outlook will be firmed up early in the year, we continue to expect high-single-digit organic services revenue growth and continued margin expansion in our projects business as we focus on driving the right work for the right customers in the right end markets.

I'll now turn the call back over to Russ.

Russell A. Becker

President, Chief Executive Officer & Director, APi Group Corp.

Thank you, Kevin. APi continues to deliver strong margin expansion across both segments, resulting in strong third quarter margins, and positioning the business to achieve 13% adjusted EBITDA margins in 2025. As I said last call, I'm confident in our leaders' ability to build on historically strong execution by delivering consistent double-digit core inspection organic growth, as well as consistently driving margin expansion across the business.

We continue to deliver margin expansion by increasing higher margin inspection, service and monitoring revenue, pricing initiatives, operational improvements and a relentless focus on customer and project selection. We believe we can create sustainable shareholder value by focusing on our 13/60/80 long-term value creation targets with a near-term laser focus on delivering adjusted EBITDA margins of 13% or more in 2025.

As we look to 2024 and beyond, we have great confidence in the business. Our backlog, our balance sheet and our ability to continue to evolve APi into an even lower-CapEx asset-light business, focused on high-margin statutorily-mandated services.

With that, I would now like to turn the call back over to the operator and open the call for Q&A.

QUESTION AND ANSWER SECTION

Operator: [Operator Instructions] Our first question comes from Andy Wittmann with Baird. Your line is open. Please go ahead.

Andrew John Wittmann

Analyst, Robert W. Baird & Co., Inc.

Q

Oh, great. Good morning, gentlemen. Appreciate you taking my question. Hey, Russ, I thought maybe I'd have you comment a little bit on the project selection and the impacts that you have here on the quarter delivering the profit dollars as expected, I think, really important point here. Can you help us understand or quantify in some way the amount of work that you might be passing on versus maybe a couple of years ago? I don't know if that's the number of proposals that are given and then accepted or how you think about that, but just something to help us [ph] pound (00:28:50) the real impact and the discipline that you're driving in that strategy?

Russell A. Becker

President, Chief Executive Officer & Director, APi Group Corp.

A

Hey, Andy, thanks for taking the time to join the call. I very much appreciate it. I have a saying that I use a lot, and volume is vanity, profit is sanity. And I have really been super impressed with the discipline that we've shown from a project and customer selection really across all facets of our business. Quantifying it would be really hard. I mean, proposal activity is really, really strong. I think that, as we highlighted, the end markets that we're choosing to play in, the activity there is solid. I mean, there is more opportunity than really there's resources to deliver on. But I would just not be able to quantify what we've been passing up.

And I mean, I feel really good about our profitability of the business. I mean, we've over-delivered EBITDA every quarter this year and raised guidance every quarter this year. And we feel really strong as we go into the fourth quarter that we'll be able to continue to do the same. But I can't tell you enough how good I feel about it, but it's just hard for me to quantify it.

Andrew John Wittmann

Analyst, Robert W. Baird & Co., Inc.

Q

Well, maybe one way to address it is, based on the comment that you had in your prepared remarks, you said the backlog is for the project businesses, which is probably where the project and customer selection is the most impactful, you said the backlog is healthy where you're not pruning. Can you talk about, like directionally, where the backlog is in total then so that we could have a better sense of the pruning impact?

Russell A. Becker

President, Chief Executive Officer & Director, APi Group Corp.

A

Yeah. Our backlog is probably – it's probably slightly down from last year, but we have two MSAs that we're currently in negotiation and expect to finalize before the end of the year. So, I would tell you that the reality of it is, on a year-over-year basis, our backlog is essentially sitting right at the same spot that it was last year. It's just that the quality of the backlog continues to improve.

Andrew John Wittmann

Analyst, Robert W. Baird & Co., Inc.

Q

Got it. Okay. Last question for me, if you would. I guess you mentioned in your script that some customer delays I guess impacted your productivity. And I guess, maybe if you could just speak to some of those delays as to what's behind them, delays is it kind of economically driven as the interest rates I think need to pencil, is it supply chain, which we didn't hear a lot of on this call, but certainly has been a factor over the past couple of years? Maybe just a little color to enlighten us on that and then I'll be done.

Russell A. Becker

President, Chief Executive Officer & Director, APi Group Corp.

A

So, the delays were primarily in our fabrication business that sits inside Specialty. And I would say that there were two fairly large delays. One was driven by a redesign with one of our data center customers. And the other one was driven by a land purchase for a very large local retail customer – you can probably do the math and figure out who that is – that they had a land purchase fall through where they were going to build a large distribution center and it delayed it.

Andrew John Wittmann

Analyst, Robert W. Baird & Co., Inc.

Q

Thank you.

Operator: The next question comes from Kathryn Thompson with Thompson Research Group. Please go ahead.

Kathryn Ingram Thompson

Analyst, Thompson Research Group

Q

Hi. Thank you for taking my questions today. Just following on the theme, and we're hearing some other companies talk about the concept of value over volume, which you have been in your journey already for much of this year and last year. As you go down that path, it's not just bidding on projects better and smarter. But could you clarify, are you seeing any changes in mix to improve that overall margin quality? So, in other words, are there certain areas or segments of inspection service that you've just decided as a firm, hey, this isn't worth it and/or are there other areas where you are increasing focus because of favorable profitability?

Russell A. Becker

President, Chief Executive Officer & Director, APi Group Corp.

A

So, Kathryn, no disrespect, but we do not use the word bid at APi, and I...

Kathryn Ingram Thompson

Analyst, Thompson Research Group

Q

Yes, understand.

Russell A. Becker

President, Chief Executive Officer & Director, APi Group Corp.

A

If there's a word that I don't like, that would be number one on my list. I have a few other ones that I can share with you sometime offline, but that would be one of them. And I would say that when I look at the businesses there, like international, we just have some poor-performing customer contracts and things like that. So, I'd say that the focus there is more around the customer and in certain cases, we've had to be aggressive about taking price under prior ownership. They weren't as focused on prices. We've been focused on price. And so, there's a little bit of end market focus, and there's also an element of just customer focus, when I think about our

international business and we continue to be able to grow that business organically, even with some of that customer pruning that we've been doing at it.

In Specialty, I would say that it's more – because our offerings in Specialty are very – fairly diverse, I would say that just across the board, it's – I like the end markets that we're in. So, I don't think it's an end market focused. It's more about making sure that we're focused just on the right client that's going to value the services that we bring so that we can actually get paid a fair price for the work that we do. The reality of it is that if we wanted to turn the spigot on, we could turn the spigot on and we could do much more work than we are doing, but the margins just wouldn't be in the same place and we would – payment terms would be different and all that other stuff that comes with that.

And so, for us, an element of this is being focused on payment terms and making sure that we're getting out in front of some of those things so that we can continue to focus on not only the 13%, but also on the 60% and the 80% free cash flow conversion, and that's a component of this as well. And then when I think about our domestic Safety business, I'd say there it's all about end markets and making sure that we're focused on the right place and really dedicating our resources to data centers, semiconductors, health care, in those end markets. So, it's a little bit different based on those three kind of buckets, but that's really how we're looking at it.

Kathryn Ingram Thompson

Analyst, Thompson Research Group

Q

Great. One follow-up. This is something that we're finding with other companies broadly in the construction value chain that with the megaprojects and the more complex, not just construction, but ensuing service of certain megaprojects, including data centers, you'll find that the end customer candidly just needs more complex needs, which means that there are only certain companies that are able to meet those needs. And so, it's disproportionately benefiting certain types of companies versus others. Would you say that, given your overall range of service and high quality, are you able to win more because of complexity of projects?

Russell A. Becker

President, Chief Executive Officer & Director, APi Group Corp.

A

I would say that there's no question that the size and the magnitude and – it's like I was on like one of our automotive customers' site just a couple of weeks ago, and when I think about it from a complexity perspective – like, I didn't think it was super complex. All right? I mean, I think that there's other end markets that are more complex. But what it is, is the scale is so great and the resources that it takes to manage and lead those types of projects is just totally different than what you would have seen, say, 10 years ago even. And so, the skill set that it takes to lead those types of project-related opportunities is just different and it takes different types of people.

And in a world where truly skilled labor is tight, you have to have the resources to be able to draw upon them. So, like on this particular opportunity, we had people from – this was – this project opportunity was in the Detroit area, and we had people that were coming up out of our South Bend, Indiana office and we're supporting our teams' efforts on this particular site. And so, you have to have some of those types of capabilities and the ability to draw on and pluck the resources out of different components of your business to support those businesses.

And the last thing that I would say there, Kathryn, is that we want to continue to have our project-related opportunities to come from the inspection service and monitoring relationships that we developed. So, we want to be in a situation where the relationship matters and that when we're proposing on these large programs, it's not based on price. Because, if they're going to base it on price, that's probably the fastest way you can get yourself in trouble on some of these larger project opportunities. I know I rant a little bit, I apologize.

Kathryn Ingram Thompson

Analyst, Thompson Research Group



Yeah, no, that's helpful. Thanks very much. I really appreciate it.

Operator: The next question comes from Jon Tanwanteng with CJS Securities.

Jon Tanwanteng

Analyst, CJS Securities, Inc.



Hi. Good morning. Thank you for taking my questions. And really nice quarter and guidance. My first one is, you mentioned strength in a number of end markets, data centers, EVs, et cetera, which is all great. I was wondering, did you see any weakness in any segments or end markets and have your consolidated growth expectations changed, if at all, especially as you prune some of these lower-quality projects out of the kind of the pipeline?

Russell A. Becker

President, Chief Executive Officer & Director, APi Group Corp.



Well, I mean, we've never really participated and played in real estate developer-led type project opportunities. Obviously, those from a project perspective, commercial office buildings, I mean, under a tremendous amount of pressure. And, again, for us, we're just fortunate that we really don't participate in those types of end markets. You hear stuff like that some of the telecommunications companies are pulling back a little bit on their capital spending and stuff. It doesn't really impact us because; number one, we're diverse geographically; and number two, we don't take these large \$500 million programs. We're doing \$30 million programs in different locations across the country. So, it really hasn't impacted our business.

One of our data center customers went through a fairly substantial – I mean, I talked about it as it relates to impacting our fabrication business, but we also had the life safety work on that particular project. And so, that impacted that component of our business. And they went through a fairly significant redesign on a lot of their data center work just because the cooling requirements have changed as it relates to their facilities.

So, I think that, in general, where the weakness is greatest is in the commercial real estate marketplace. And there's going to be some weakness in retail, in general. And you've seen some pullback from like Amazon with their distribution centers and things like that. But that's, again, not areas that we really had a high participation rate.

Jon Tanwanteng

Analyst, CJS Securities, Inc.



Okay. Great. And then, just, should we expect a bigger focus on international M&A as you improve the structure at Chubb? What would be the timing of that, number one; and is the pipeline of opportunities you see out there as good as what you see domestically in terms of valuation, number of opportunities, all that stuff?

Russell A. Becker

President, Chief Executive Officer & Director, APi Group Corp.



So, we've been really focused on the integration of the business. There's been some opportunities that have come across the transom that we've passed on. Some of that has to do with the distraction factor, and we want them to stay laser-focused on Chubb value capture plan of \$100 million, which is on track. But the opportunities are equally as good in that market as they are here in the US. And I suspect that you'll see us get to be a little bit more active in the space as soon as next year.

Jon Tanwanteng

Analyst, CJS Securities, Inc.

Got it. Thank you, Russ.

Q

Russell A. Becker

President, Chief Executive Officer & Director, APi Group Corp.

Thanks, Jon.

A

Operator: The next question comes from [ph] Andy Kaplowitz (00:43:13) with Citi. Please go ahead.

Natalia Bak

Analyst, Citigroup Global Markets, Inc. (Broker)

Hi. Good morning. This is Natalia Bak, on for Andy Kaplowitz. So, I was just wondering if you could provide a little color regarding your progress on improving cash generation? You obviously are generating a lot more cash here today and maintain your outlook of 65% free cash flow conversion. And maybe if you could provide a little color on supply chain condition that you're seeing?

Q

Kevin S. Krumm

Executive Vice President & Chief Financial Officer, APi Group Corp.

The last part of that question – good morning, [indiscernible] (00:43:42) – this is Kevin – was supply chain, I think. If not, then you can correct me at the end.

A

So, our cash flow profiles continue to improve this year, both from an absolute delivery standpoint as well as a conversion standpoint. As we started the year, we're laser focused primarily on working capital rate and to a lesser extent CapEx. As we moved through this year, the changes we made in the business that we've been talking about, whether it's a higher mix of service or continued disciplined customer and project selection, are bearing fruit both in working capital rate on a year-to-date basis sort of vis-à-vis where we ended or vis-à-vis prior year, as well as conversion.

And from a supply chain standpoint, we are largely behind the impact of supply chain that we talked about last year in the first half of the year that drove a significant working capital rate investment.

Natalia Bak

Analyst, Citigroup Global Markets, Inc. (Broker)

Great. Thank you. Very helpful color.

Q

Operator: The next question comes from Parth Patel with JPMorgan. Please go ahead.

Parth Patel

Analyst, JPMorgan Securities LLC

Hi. Good morning. Thanks for taking my question. In Specialty, organic growth was down in the quarter on a tough comp. What was pricing there, and was there any impact from commodities flowing through?

Q

Kevin S. Krumm

Executive Vice President & Chief Financial Officer, APi Group Corp.

A

So, on the Specialty business, we did not break out organic growth this quarter sort of volume versus price and price pass-through. The primary reason is while we continue to get pricing on the service side of the business, the material cost de-escalation that we saw year-on-year drove a significant revenue rate reduction in the quarter. So, we faced year-on-year that material cost de-escalation drives a headwind at revenue rate, which is what you saw in the quarter in the Specialty business. So, underlying, we continue to get pricing on the service side of that business. We just faced that headwind at revenue from the material cost de-escalation.

Parth Patel

Analyst, JPMorgan Securities LLC

Q

Great. That's very helpful. And then, just a follow-up, can you give an update on some of your big union agreements? I think the last one was negotiated back in 2020. Just any update there?

Russell A. Becker

President, Chief Executive Officer & Director, APi Group Corp.

A

Well, the largest union agreement that we have is with what we call the Road Fitters Local 669. I think we have another 18 months before that agreement will be renegotiated. We have no concerns about our ability to renegotiate that agreement and feel really good about it. So, there's some smaller ones that are coming up and really, if you kind of cycle through them on it every year, there's different agreements that come up. But the largest one that we're signatory to comes up in 18 months, roughly.

Parth Patel

Analyst, JPMorgan Securities LLC

Q

Great. Thank you so much.

Operator: It appears we have no further questions at this time. I will now turn the program back over to our presenters for any additional remarks.

Russell A. Becker

President, Chief Executive Officer & Director, APi Group Corp.

Awesome. Thank you. In closing, I would like to again thank all of our team members for their continued support and dedication to the business. We believe our people are the foundation on which everything else is built. Without them, we do not exist. I'd like to thank our shareholders, our long-term shareholders, as well as those who have recently joined us, for your support. We appreciate your ownership of APi, and we look forward to updating you on our progress throughout the remainder of the year. Thank you for taking the time to join the call this morning, everybody.

Operator: This does conclude today's program. Thank you for your participation. You may disconnect at any time.

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