ATS Automation Tooling Systems, Inc.

First Quarter 2023 Conference Call and Webcast

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PRESENTATION

Operator

Good morning, ladies and gentlemen. Welcome to the ATS Automation First Quarter Conference Call and Webcast. This call is being recorded on August 10, 2022 at 8:30 a.m. Eastern time. I'll now like turn the call over to David Galison, Head of Investor Relations at ATS.

David Galison — Head of Investor Relations, ATS Automation Tooling Systems, Inc.

Thank you, Operator, and good morning, everyone. On the call today are Andrew Hider, Chief Executive Officer of ATS; and Ryan McLeod, Chief Financial Officer.

Please note that our remarks today are accompanied by a slide deck, which can be viewed via our webcast and available at atsautomation.com.

We caution that the statements made on the webcast and conference call may contain forward-looking information, and our cautionary statement regarding such information, including the material factors that could cause actual results to differ materially from the statements and the material factors or assumptions applied in making the statements, are detailed in Slide 2 of the slide deck.

Now, it's my pleasure to turn the call over to Andrew.

Andrew Hider — Chief Executive Officer, ATS Automation Tooling Systems, Inc.

Thank you, David.

Good morning, ladies and gentlemen, and thank you for joining us.

Today, ATS reported another quarter of profitable year-over-year growth. This quarter also featured record revenues, order bookings, and order backlog, all delivered in a challenging and fluid economic and business environment. Our results reflect our focus on strategic markets and the ongoing application of the ABM playbook by our dedicated global teams. As part of our Expand strategy, integration activities progressed with all of our acquisitions from last year, and we remain on target with our goals.

Today, I will update you on the business and Ryan will provide his financial report.

Starting with our financial value drivers.

Q1 revenues were a record $611 million, up 20 percent from last year, driven by a combination of acquired businesses and continued strength across our core operations. Organic revenue growth was 6 percent year-over-year.

Order bookings for the quarter were $736 million, up 16 percent year-over-year, and featured key wins in both life sciences and transportation.

Our Adjusted EBIT margin in Q1 was 14.3 percent.

Moving to our outlook.

We finished with approximately $1.6 billion of order backlog that includes several large enterprise programs with long durations, providing a solid base of business. Our backlog remains distributed across diversified, regulated industries where quality and reliability are mandatory.

By market, in life sciences, conditions have remained generally positive, with good activity in key sub-markets, including medical devices, as well as pharma and radiopharma. Life sciences represents nearly 50 percent of our ending backlog, and it remains a key vertical for ATS.

In EV, OEMs continue to drive their investment plans forward. We expect ongoing demand for EV automation, as global capacity at OEMs is well below the levels required to meet the stated production targets. Despite strong growth to date, the EV industry is in the early stages of its investment cycle. During the quarter, we received an initial US$70 million EV order from an existing global automotive customer for battery assembly systems in their Canadian and U.S. manufacturing operations. This order is part of a multi-phase enterprise program. The OEM selection of ATS as its trusted partner to support their EV strategy demonstrates our expertise and successful track record as an industry leader in delivering solutions to address evolving battery technologies.

In food and beverage, we continue to see requests for increased automation. Demand for our Apollo evaporators and other energy-efficient products remains strong, and we're seeing more projects and opportunities in food and liquid food and a pickup in beverage.

In energy, high energy costs and a heightened focus on emissions supports ongoing interest in nuclear power. We are also seeing growing demand for grid battery storage, as renewables are playing a more significant role. ATS is positioned to participate in both areas.

In consumer, we're seeing an ongoing recovery in the personal care and cosmetic sector, which was particularly hit hard by pandemic-related effects.

In services, we've further evolved our lifecycle portfolio. As an example, in Q1, we refreshed our integrated bundles, which are designed to increase customer touch points and generate recurring revenue.

We're driving continued collaboration and execution of the aftermarket strategy across all parts of our business, including acquired businesses. Teams are focused on leveraging our regional networks for customer support, as well as exploring the use of Illuminate and other tools to enable digital insights and capabilities.

Costs and wage inflation, supply chain constraints, and the ability to attract and retain high-end talent remained ongoing challenges in Q1, and the situation remains dynamic for ATS and our customers. With the dedicated focus and efforts of our teams and the deployment of our ABM, we are working to create further agility within our businesses to respond. To date, we've had a good level of success in mitigating some of the challenges. However, as I stated in Q4, we are not immune.

That said, these challenges are also impacting customers and generally play to our favour, as higher costs could be the tipping point making the ROI more attractive for automation, assuming end market demands remain. ATS is ideally-positioned to assist our global customers with automation solutions that will strengthen their global supply chains and reduce both production costs and labour dependence.

In Ukraine, we're supporting our team there, and some of our employees have returned to work on a semi-regular basis with their safety being of utmost importance to us. The war in Ukraine also continues to create global, geopolitical, and economic ramifications.

In addition to the situation in Ukraine, other macro concerns create ongoing challenges for us to tackle throughout the remainder of the year.

Moving to ABM highlights for the quarter.

We remain focused on expanding our approach across all parts of the business. Our ABM playbook is part of our competitive advantage and has helped us stay ahead of the quickly-evolving and challenging economic environment, and creates a common language for all of our teams to use.

Our biggest focus in Q1 continued to be on improving supply chain issues, cost effectiveness, and reduction of lead times. During the quarter, our divisions ran many successful kaizen and problem-solving events, while participation in our ABM boot camps was strong.

In addition, we held our ATS Leadership Conference in person for the first time since 2019, as leaders from across the business gathered together. The ABM was one of the central themes from the event. I was encouraged to hear from a variety of leaders across the organization as they showcased best practices and shared their experience on the continuous improvement journey.

We are proud of the ongoing commitment to the ABM, and its strength as our playbook is more evident than ever during these challenging times.

On M&A, our integration of previous acquisitions across the business are progressing to plan, and we are actively cultivating our funnel. Overall, our funnel remains robust moving into Q2.

On integration activities, I would like to offer a few ongoing examples of the collaboration we're seeing with our teams.

Comecer, along with one of our SP teams in Spain, have been working together on integrating Comecer isolators with SP machines, and have won their first project which was kicked off in Q1. We've also leveraged SP's channels to win a second booking through IWK with a cartoning solution.

Building off the success of one of our Q4 President's Kaizen events, our life sciences synergy funnel has continued to grow, and as we noted previously, our services team is working closely with acquired businesses to share strategy, tools, and technology. We are encouraged by our team's focus and efforts on integration activities.

On sustainability, we look forward to sharing our third Annual Sustainability Report later this year. ATS has adopted various initiatives and policies addressing ESG factors relevant to the Company, its employees, its suppliers, its customers, and the community as a whole.

As an example, sustainability in packaging is increasing in importance with our customers, and oftentimes, providing an innovative packaging solution, along with automation capabilities, increases our likelihood of winning business with some of our customers. We are developing an initial packaging confidence centre at IWK, which is expected to be completed in the fall.

On innovation, our teams consistently impress with their dedication to developing new applications in our key markets.

A few highlights from Q1.

Our innovation team in Cambridge, along with Illuminate, launched new machine learning insights to the base Illuminate product.

We demonstrated Symphoni and launched collaborative functionality for SuperTrak GEN3 at the Automatica show in Germany. This functionality enables an employee on the production line to work hand-in-hand with the machine in a safe environment.

Our Comecer team showcased a new solid target processing system at a nuclear medicine industry event in June, and as an update to a topic I spoke about it briefly in Q4, BioDot completed commissioning of an integrated demo unit that combines an SP lyo and the BioDot LyoBead dispensing unit.

In summary, we are pleased with our record order bookings and backlog, and are encouraged by our Q1 performance, while, at the same time, we remain focused on countermeasures to mitigate risks, with special ongoing attention to supply chain. Our results demonstrate the strength and growth of our portfolio and offerings and the dedication of our global teams. As we execute on our strong backlog, we will continue to move forward with our strategy and build flexibility into our business. This will be assisted by our ABM as we deliver results for our customers and shareholders every day.

Now, I will turn the call over to Ryan.

Ryan, over to you.

Ryan McLeod — Chief Financial Officer, ATS Automation Tooling Systems, Inc.

Thank you, Andrew, and good morning, ladies and gentlemen.

This morning, I will start with a review of our Q1 operating results, and then provide further details on our balance sheet.

Beginning with orders, bookings were $736 million, up 16 percent compared to Q1 last year. Growth was driven by acquired companies contributing 12 percent of the increase, primarily from SP. Organic growth in bookings was 5 percent, partially offset by a 2 percent headwind from foreign exchange translation. Organic growth included the initial order booking for US$70 million from an existing global automotive customer that Andrew referenced in his remarks. Recall that in Q1 last year, we reported a $120 million life sciences order booking. Our trailing 12-month book to bill ratio at the end of Q1 was 1.12 to 1.

On Q1 revenues of $611 million, our top-line growth was 20 percent over last year. Organic growth of 6 percent related primarily to increases in the transportation and consumer verticals. Foreign exchange translation created a 3 percent headwind compared to Q1 last year. Acquired companies added 17 percent to revenue growth, with SP being the primary contributor.

We remain focused on growing our after-sales services business, which grew 42 percent year-over-year, including 34 percent organic growth compared to Q1 last year.

Our Q1 ending backlog of $1.56 billion was 25 percent higher than Q1 last year.

Looking ahead, our revenue conversion for Q2 is estimated to be at the higher end of the 35 percent to 40 percent range of order backlog. Given the composition of our backlog and the stage of some of our enterprise orders, the expected conversion has moved back to this range for Q2. As a reminder, this estimate is based on revenue expectations for both the execution of projects from backlog and work that will be booked and billed within the quarter.

Moving to margins, included in Q1 gross margin were $5.2 million of costs related to fair value adjustment of inventories acquired through acquisitions. Excluding these amounts, Q1's gross margin was 28.7 percent, 50 basis points higher than the comparable period last year. Higher year-over-year gross margin reflected increased after-sales service revenues and other continuous improvement efforts achieved by deploying our ABM. Sequentially, our gross margins declined in the first quarter, as we have seen some cost pressure due to supply chain inflation and a shift in our current mix of business following the completion of some higher-margin enterprise projects.

Despite this decline in margins, our operations continue to execute well. Managing cost increases and lead-time extensions in our supply base remains an important point of the focus for our teams. While we have seen some recent stabilization in commodity pricing and some pockets of improvement, overall costs remain high, and we expect it will take some time for cost reductions to positively impact our business. Electrical components, mechanical parts, and custom fabricated parts all saw further lengthening of lead times in the quarter, and we remain actively engaged with our supply base to mitigate these risks.

In the quarter, we completed nine supply chain-related ABM events, including savings funnel workshops, as well as kaizen and problem-solving events. Our countermeasures continue to include embedding secured supplier costs into new quotes, accelerating vendor order timing, securing alternative sources of supply, and implementing pricing changes.

Moving to SG&A, expenses were $27.6 million higher than Q1 last year. This year's costs included $20.3 million of acquisition-related amortization and $0.4 million of acquisition-related transaction costs. Excluding these comparable items in both periods, Q1's SG&A was $91.5 million, $21.8 million higher than last year, reflecting incremental SG&A costs from acquired companies, primarily SP and NCC.

First quarter stock compensation recovery was $4 million, down $12.8 million from stock compensation expenses of $8.8 million last year. The decrease is a result of a revaluation of deferred and restricted share units.

Q1 adjusted earnings from operations were $87.5 million or 14.3 percent compared to $65.4 million or 12.8 percent last year. The increase reflected improved gross margins and stock compensation recovery, partially offset by higher SG&A expenses.

CFT improved on a year-over-year and sequential basis. Excluding CFT, our core business again operated in line with our expectations.

Moving to the balance sheet.

In Q1, cash flow used in operating activities were $31.7 million. Cash usage was primarily related to the timing of investments in non-cash working capital driven by project execution timing and

customer billing milestones. Our non-cash working capital as a percentage of revenue was 11.4 percent in Q1, up from 8.2 percent in Q4. As a reminder, our target is to remain less than 15 percent, and this is unchanged despite variations like this quarter-to-quarter. In the short term, we expect working capital to remain above 10 percent as we work through program milestones.

We invested $12.4 million in CAPEX and intangible assets in Q1 compared to $14.3 million in Q1 last year. Our CAPEX investments are on plan for this fiscal year. However, we have built in flexibility to our plans to adjust as needed. As a reminder, on capital allocation, we remain focused on internal capital deployment and M&A, followed by our share buyback, which we use opportunistically through our normal course issuer bid. During the quarter, we were active with the NCIB, and purchased 609,000 common shares for $20.7 million.

On leverage, our quarter-end net debt to Adjusted EBITDA ratio was 2.8 to 1. On a pro-forma basis, including the trailing 12-month EBITDA contributions of acquired businesses, our net debt to Adjusted EBITDA ratio was approximately 2.7 to 1.

We ended the quarter with $140 million of cash and availability on our credit facilities of approximately $195 million.

Going forward, continue our focus on maintaining our strong balance sheet, while also supporting flexibility in our financing structure to continue pursuing our growth strategies.

In summary, we're pleased with another quarter of solid results. These achievements reflect organic growth, contributions from acquired businesses, and the ongoing deployment of our ABM

playbook in a challenging environment. We're prepared to continue to operate in this environment, with cost inflation and lead-time pressures in our supply chain throughout the remainder of the year. We expect ABM efforts, combined with our strong order backlog, will continue to serve us well in managing these challenges. Our global teams remain committed to delivering best-in-class solutions to our customers, along with strong financial results for our shareholders.

Now, we will open the call to questions from our analysts.

Operator, could you please provide instructions? Thank you.

Q & A

Operator

We will now take our first question from David Ocampo from Cormark Securities. Please go ahead.

David Ocampo – Analyst, Cormark Securities, Inc.

Thanks. Good morning, everyone.

Andrew Hider

Good morning.

Ryan McLeod

Good morning.

David Ocampo – Analyst, Cormark Securities, Inc.

Andrew, I think you talked a little bit about uncertain market conditions that may potentially delay orders flowing through to your backlog, but I was wondering, for the contracts that are currently in backlog, are there any risk of delays on delivery or even potential cancellations just given those—given the uncertainty in the market right now?

Ryan McLeod

Hi, David. This is Ryan. I'll start and Andrew can certainly add in. We're not seeing anything out of the ordinary in our backlog or seeing any heightened risks of cancellation or anything like that. Typically, our contracts do allow customers to cancel, but they would also be required to compensate us for any work completed, so nothing material. We see normal course scope changes, as we typically do, but we have not seen any change that would impact our order backlog to date.

Andrew Hider

David, to address the first part of the question, just to (inaudible) where we are today, best bookings quarter in Q1 we've had ever and our funnel remains healthy. As we look at the markets, and you've known this story, but we've focused on markets that we view are more resilient during challenging times, and so while we're being certainly cautious, we are cautiously optimistic around how we view the market and the value that we, ATS, and automation can play as customers are looking at

their dynamics and the situation they (inaudible), so I would characterize my conversations as being just that when I'm having discussions with customers.

David Ocampo – Analyst, Cormark Securities, Inc.

Okay, that's helpful, and then for your automotive business, particularly EV, how should we be thinking about the growth there? I don't think you've laid it out in the past. Is it something similar to life sciences where it could be high-single digit just given the supply/demand balance that's out there, and maybe as a follow-up to that, how is competition in the automation space for EV?

Andrew Hider

Yes, so I'll walk both of those specifically, and look, I'll hit the competition piece, so there is competition. It's a different competition level, as these are generally very large pieces of equipment, and we, ATS, a little over five years ago, we shifted our focus on the EV space, and we've been in this market for over a decade now and we have technology. We've got capability. We've got experience, and really a strong track record of performance in this area, and to be very specific on it, it's around battery pack assembly and (inaudible), which, when you look at customers making the shift, that is one of the critical areas and strategic areas that they focus on to get right, and I've talked about it in the past around the number of welds, and if one weld goes wrong, what it means to the EV longevity, but it is a very strategic area, and so the growth rate in this market is fairly significant, and we used the phrase around bullish of the market in last quarter and reviewed that this market has certainly a long tenure for getting the ability to meet capacity to meet demand, and so ATS is well-positioned to support and help through this market.

David Ocampo – Analyst, Cormark Securities, Inc.

That's helpful commentary, Andrew. Thank you. I'll hop back in the queue.

Andrew Hider —

Appreciate it.

Operator

We will now take our next question from Mark Neville from Scotiabank. Please go ahead.

Mark Neville – Analyst, Scotiabank

Hey, good morning, guys. If I could maybe just pick up first on the after-sales growth, I think you said—quoted 32 percent organic in the quarter. Can you maybe just—I think that's the highest rate of growth that I recall you guys talking to, so can you maybe just speak to some of the drivers behind that, if that's accelerating with some of these acquisitions? Just a little more detail around that, please.

Ryan McLeod

Yes, so Mark, just to clarify, it's 34 percent organic growth in the quarter, and so this is an area that we've invested in in terms of building out our capability, our ability to service customers. We've talked about different lines. We've expanded our regional presence, so all of those have factored in.

Andrew Hider

Yes, and Mark, just to walk through this, and Ryan touched on it, but we've invested around, really, capability within the region and solutions that we can provide for customers, and I highlighted one on the call, but to be more specific on that, we're now looking at the full—not to say we haven't in the past, but we're looking at solutions on the full lifecycle of our equipment, whether it's new or in existence, to really help our customers through operating at a more efficient level, and so we can now take the data from Illuminate, from other insights, and bring the ability to have a more efficient system, and our teams, with the investment around the marketplace, with ordering, with ability to monitor machines, ability to improve efficiency, can really pivot and help our customers through that transition.

Lastly, what I'll just note is what we saw for the last two years is services going from a nice to have to really mission-critical for our customers, and obviously, our teams really look at this as a certainly strong proof point in the direction, but it's early days and more to come, and we're seeing this with new acquisitions, as well as with our continuation on our business today.

Mark Neville – Analyst, Scotiabank

Just to follow on to that, I think the target was 20 percent. Just curious if you're willing to update that now, or—but again, it just feels like with the growth and some of your comments that it's probably—feels like a higher number?

Andrew Hider —

At this time, we're not updating it, and here's why, and when we look, we view this as strategic and a focus area across ATS, and when you step back and look within our businesses, we have

businesses that are close to 40 percent, and we expect them to continue their progression and offer new digital solutions, new insights, new capabilities that really help customers, and we have businesses that are below our target, and so it really is that progression to get there, and it's not going to be an area that we slow down once we get to that level.

Mark Neville – Analyst, Scotiabank

Got it. Just maybe on lead times, you spoke to an increase for certain components, electrical/mechanical components. I'm just curious how you're managing that and what you do in the event that you're maybe short on a component or—and then there's, potentially, maybe people that are, I don't want to say stranded, but need to be shifted around, so just curious what you're doing, how you're managing it, and—yes, maybe start there.

Andrew Hider —

Yes, so this is an area that I would say the ABM has really been a key focus for us and just—close to a year ago, our teams really saw this starting to take shape and see the challenging environment, and they implemented very quickly a daily visual management process and pretty much across the corporation, and what that allows us to do and our supply chain teams to do is really identify those critical elements, those critical parts or shortages and have a very proactive or reactive approach to that.

It allows us to then say, okay, how do we expedite, how do we get this on-site, where we can draw from, and because we've invested in systems and solutions globally, we even shift around within divisions if we have the ability to, and so we've taken a daily visual management approach, which allows

us to understand where we have the impact. We oftentimes know in advance that something is going to be short and we can take countermeasures and take operational measures to really mitigate that impact on ATS, and so while it's a challenging environment, our teams have done an excellent job of operating in this environment.

Mark Neville – Analyst, Scotiabank

Yes, I agree. It's quite impressive, so good on you guys. Maybe just my last question just on M&A, your stock has been pretty volatile year-to-date. I think you started the year closer to 50, dropped to 30, now it's back into the 40s. I'm just curious how you view your multiple, your share price in the context of M&A and your willingness to do M&A, or—yes?

Andrew Hider —

Mark, why don't I start, and then Ryan can certainly add in around where we see our multiple, our trading multiple, but look, our funnel is healthy here, and I will often talk about ABC, always be cultivating. We are constantly cultivating, and the markets that we view are most attractive for ATS long term, and really creating long-term shareholder value, and so we continue to operate in that environment.

Our funnel is made up of small, medium, and large potential. That said, we're extremely disciplined, and we continue to ensure that it's the right value creation for ATS long term, and so, certainly, it's been an ongoing evolution and one that we view that we want to continue to drive.

Ryan McLeod —

Yes, I would just add, we've seen a reset in multiples across the board, but generally speaking, I would say we view ours as undervalued versus others in our space.

Mark Neville – Analyst, Scotiabank

All right. Thanks for the time, guys. Again, great job.

Andrew Hider —

Thanks, Mark.

Operator

We will now take our next question from Justin Keywood from Stifel GMP. Please go ahead.

Justin Keywood – Analyst, Stifel GMP

All right. Good morning. Thanks for taking my call. I was hoping to square the record bookings and backlog with the guided revenue conversion for Fiscal Q2, which I believe implies a bit of a pause in organic growth, and if that's just a function of project timing and if we should expect the growth to ratchet back up in the second half of the year, or any commentary around that?

Thanks.

Ryan McLeod —

Yes, so Justin, first of all, we do make this assessment every quarter, and it's based on our portfolio of projects that are in our backlog as well as our expectations for in-quarter bookings and revenues. We do expect in this quarter to be in the higher end of that 35 percent to 40 percent range of backlog, and really, what we're seeing is—and I talked about this a little bit, but we've had some larger enterprise projects recently get completed or get close to completion, and while we have new ones in our backlog, they're in the early stages of their overall schedule, and what happens is, during those design phases before projects hit the build stage, it's relatively lower revenues that get produced during those phases, so it's—that's really what's driving the lower conversion rate in this quarter, and it's certainly nothing new.

Over the long term, as I've talked about, given the change in our business make up, we've added more product sales, we've increased services, we've added more original equipment, we do expect to typically operate into that 40 percent to 45 percent range, but this is more just reflective of our current portfolio and backlog of projects.

Justin Keywood – Analyst, Stifel GMP

Got it. That's helpful, and has there been any change in expectation for organic growth in the short or medium term? I know ATS always strive to hit organic growth above the industry average.

Andrew Hider —

There is no change, and as you're well aware, we've targeted markets that we view are generally more resilient in these times.

Justin Keywood – Analyst, Stifel GMP

Got it, and then just finally on margins, we saw a nice improvement in the quarter year-on-year, and I know this has been a big part of the ABM. At this point, are you anticipating any additional margin expansion, realizing the backdrop is pretty challenging, but is there an opportunity to still improve margins higher than the 500 bps goal, which has been essentially achieved?

Ryan McLeod —

If we just step back, I'll walk through the different components.

We are pleased with where we operated this quarter year-over-year. We had expansion sequentially. I talked about some of the issues in our gross margin or some of the factors that affected our gross margins. We did see some challenge, and supply chain has been a headwind. As Andrew said, our teams have executed very well in this environment, but it is a headwind, and we also saw some challenge from mix in our programs, and as I just talked about, with the revenue flows, we had some higher-margin enterprise projects that were completed and newer enterprise projects are in the early stages of completion today.

Going forward, we still have our focus on margin expansion. It is challenging in the short term, but we do have a continuous improvement focus to our ABM, and we're confident in our ability to continue to perform well, both in the short term, and then ultimately drive margin expansion as the environment improves.

Justin Keywood – Analyst, Stifel GMP

Thank you for taking my questions.

Operator

We have a follow-up question from Mark Neville from Scotiabank. Please go ahead.

Mark Neville – Analyst, Scotiabank

Hey. Thanks again, guys. Maybe just on the macro, I'm just curious if you're doing any internal exercises just in the event that there would be a slowdown or running any ABM around that; what you can do, and if there would be—just curious if there's any change to the CAPEX budget for the year. Thanks again.

Ryan McLeod —

Yes, so Mark, we're obviously aware of the risk and what's happening in the environment, and as part of our normal course, we do discuss and develop contingency plans. As Andrew said, we're cautiously optimistic at this point that our verticals will be resilient, and automation is going to continue to be an area that companies invest in to drive efficiency growth in their businesses, but that doesn't mean we would be immune to the effects of a recession or something similar, so we have a good, strong backlog. That gives us visibility, time to react.

We've also built flexibility into our cost structure. We operate with a mix of leased and owned facilities. We operate with approximately 10 percent of our workforce through subcontractors, and that

helps us manage utilization and workflow, and that's part of how we operate as a project-based business. We have flexibility in other areas of our cost structure as well.

In terms of CAPEX, we do want to maintain investment in innovation, but we do have flexibility in other areas to ensure that, again, we're being competitive and efficient in our cost structure, so as I said, we have a more resilient end market mix today. We've also lowered our exposure to CAPEX where we've increased services, increased our product revenue, so we're comfortable that, if conditions deteriorate, that we both have a strong platform and the ability to react quickly.

Mark Neville – Analyst, Scotiabank

Got it, and maybe just to focus specifically on Europe, obviously there's a heightened risk with some of the economic data coming out of there, and energy prices as well, so maybe just, again, a little more colour around your conversations with customers in Europe; if they're any different than other parts of the world, and the second part if energy price is a big part of the cost structure for you and a risk. Thanks.

Andrew Hider —

Yes, so two questions, there. I'll take the customer discussion.

I would say we have not seen a marked difference in discussions with customers to date. We do view this as an opportunity and one of the areas we're driving expansion on certain key markets and verticals for ATS, and so we have not seen a marked difference to date in the discussion, in the general

tone with customers. That said, you're going to have multiple different conversations based on the markets that we're serving, but in general, I would say there is not a big difference.

The second part of the question, we really looked at our business as a whole in this energy dynamic and what would happen, and so our teams have taken a proactive approach around what would happen if this were to happen, and just to give you a reference point, Germany energy from natural gas, a little over 20 percent from Russia. If that were to be shut off, we have started to build out plans on what our countermeasures or what our reaction would be to that, and while it's never perfect when we are in planning mode, we're certainly starting the process to ensure that we could think about and walk through how we would continue to deliver for our customers and continue on a safe operation during that environment, so yes, it has been part of our planning process. Yes, we've been going through what the actions we'd take in that situation and how we'd continue to support our customer base.

Mark Neville – Analyst, Scotiabank

Thanks, and would energy—would the energy cost be significant? Is it a big part of the cost structure for you in Europe? I don't how much your facilities consume, if it's material or not.

Andrew Hider —

That cost structure would be part of our consideration and ongoing, and we've built many of that thinking into our business. That said, the real discussion that we've seen a lot—real drive around is the natural gas coming from Russia and what would happen if that were to be shut off, and so that has been

a bigger focus, and so not to get into breakdowns of every country in every region and their energy usage, but it's been one of the ones we've been looking to countermeasure.

Mark Neville – Analyst, Scotiabank

Got it. Thanks again for all the time. Appreciate it.

Andrew Hider —.

You bet.

Operator

We will now take our next question from Maxim Sytchev from National Bank Financial. Please go ahead.

Maxim Sytchev – Analyst, National Bank Financial

Hi. Good morning, gentlemen.

Andrew Hider —

Good morning.

Ryan McLeod —

Good morning.

Maxim Sytchev – Analyst, National Bank Financial

Andrew, was wondering if you don't mind providing a bit of an update in terms of integration process on SP Industries and CFT. Obviously, different type of transactions, but if you don't mind providing a bit of an update on both. Thanks.

Andrew Hider —

Yes, sure, and I'll start with the headline and then I'll—but I'll piece it apart. Both on plan, on target, and I highlighted this a little bit, and I'll hit SP to start.

One of the areas that we're very, very pleased with is the synergy funnel and execution, and it was one of the thesis around why we very much like this business, and we've seen really performance towards that with Comecer and their isolation, as well as the business in Spain with SP called i-Dositecno, really coming together and bringing that solution to a new customer, as well as SP having the ability to pull through other businesses like IWK, and so the team has done an excellent job around that ability to bring the value to market, and just to highlight the other aspects, they're on plan with their integration. They've really just taken on the ability to be the ABM in a very focused effort. A lot of folks have gone through the ABM boot camp, and so, in general, I would say we're pleased with the progress, and certainly look forward to this being a real target area for ATS moving forward.

As we look at CFT, same commentary. This business, the team took to the ABM to drive efficiency, to drive how they view their approach to market, to really bringing the value that they can bring to customers and making that the forefront of the conversation, plus stepping back and looking at

their cost structure and taking critical and clear action to ensure their cost structure is aligned with the value that they can create, and so while we're continuing to drive synergies from a market perspective, we're very pleased with the progress on both of those organizations.

Maxim Sytchev – Analyst, National Bank Financial

Okay, very helpful. Thank you, and then just one last question in terms of supply chain; obviously some of the peers in the space have started to say that things at least are not getting worse. I'm just curious, I know that you highlighted the electrical components being still in tight supply, but how should we think about this as the year progresses? At what point do you think that will get better, and how should we think about the impact on you guys, specifically? Thanks.

Andrew Hider —

First, we view this as being with us for the remainder of the calendar year, and so our teams have been very focused on not letting off on the daily visual management and ensuring that we can have continuity and continuation of our operation.

Number two, we have seen some areas stabilize, and Ryan walked through that, while we've seen others be more challenging, and so I do—when we step back and look at the way we've performed, I think that we've performed very well, but we're not taking our foot off the gas pedal here, and we do think this is going to be a dynamic environment for the remainder of the year and one that we have to continue to utilize the ABM to outpace and really drive value in the markets we serve.

Ryan, is there anything you would add on to that?

Ryan McLeod —

Maybe just a point of clarity, so year-over-year, we've certainly seen cost inflation in our supply base. Sequentially, we have seen things start to stabilize now. It's very dynamic. We've seen pockets of improvement in certain commodities. Other components have still got—had sequential increases, but generally it's been more stable sequentially, and then as I noted, lead times in some areas have extended in this quarter, particularly in electrical components, so as Andrew said, it's dynamic, but our mitigation efforts have been, we believe, very effective and it's helped us to navigate this period.

Maxim Sytchev – Analyst, National Bank Financial

Okay, and then, actually, just to clarify, are price increases part of the toolbox that you're using with customers right now to offset that inflationary dynamic?

Andrew Hider —

Yes. Yes, we have built out a commercial ABM and price is part of that process.

Maxim Sytchev – Analyst, National Bank Financial

Any push back, Andrew, in terms of those price increases that you're passing through, or what's been the conversation with the clients?

Andrew Hider —

In large part, look, we're a high value to our customers, and then we look at what we can create and how we can help customers create their solutions to market. They generally understand the situation and generally really view ATS as a key enabler, so while we don't view this as zero pushback, we generally think it's a high-value solution for customers.

Maxim Sytchev – Analyst, National Bank Financial

Okay, excellent. That's it for me. Thank you so much.

Operator

We have no further questions. Back to you, Mr. Hider.

Andrew Hider —

Thank you, Operator.

We look forward to staying focused on our goal of creating value for our customers and shareholders alike as we continue to execute, and just before we conclude, we'd like to remind everyone that we will host our virtual Annual Meeting tomorrow beginning at 10:00 a.m. Eastern.

Thank you for joining us today. I look forward to speaking to you on our Q2 call in November. Stay safe and goodbye for now.

Operator

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