NASDAQ:CECO Q3 2026 Earnings Call Transcript

Generated on 11/25/2026

Conference Operator | Operator:

Good day, and thank you for standing by. Welcome to the SECO Environmental third quarter 2026 earnings call. At this time, all participants are in a listen-only mode. After the speaker's presentation, there will be a question and answer session. To ask a question during the session, you will need to press star 11 on your telephone. You will then hear an automated message advising your hand is raised. To withdraw your question, please press star 11 again. Please be advised that today's conference is being recorded. I would now like to hand the conference over to your speaker today, Marcio Pinto, Vice President of Corporate Integration and Investor Relations. Please go ahead.

Marcio Pinto | Vice President of Corporate Integration and Investor Relations:

Good morning, and thank you for joining SECO Environmental's third quarter 2026 earnings call. With me today are Todd Gleason, Chairman and Chief Executive Officer, and Peter Johansson, our Chief Financial Officer. Our earnings release and presentation include the relevant disclosures and non-GAAP reconciliations, and they're available on our investor relations website. Today's discussion includes forward looking statements, including our 26 and 2027 outlook and preliminary 2028 expectations, which are subject to risks and uncertainties, including those described in our SEC filings and in our presentation. We will discuss also non-GAAP financial measures. Please refer to the reconciliations and definitions in the presentation and appendix. Our reported results include Thurmond from the June 1st acquisition date, and this quarter includes a full three months of Thurmond's financial performance. Todd will begin with our business performance. Peter will then review financial results and update a 26 outlook, and then Todd will return to discuss our initial 2027 outlook and preliminary 2028 view. We will then open the call for questions. With that, I'll turn it over to Todd.

Todd Gleason | Chairman and Chief Executive Officer:

Thank you, Marcio, and good morning, everyone. Let me start by saying thank you to our global SECO teams for another outstanding quarter. It certainly is a very dynamic time with tremendous change, global investments in industrial infrastructure, and a fast-paced information environment. What remains consistent is SECO's high-performance results. Let's review. Please turn to slide number three. The overall takeaway is we had another quarter of record results and our 2027 outlook points to even more tremendous results ahead. In the third quarter, we delivered revenue of approximately $404 million, adjusted EBITDA of $70 million, and an adjusted EBITDA margin of 17.3%. Revenue more than doubled and adjusted EBITDA roughly tripled when compared against third quarter of last year. Legacy Seco performed very strongly with organic revenue growth of 30% and adjusted EBITDA growth of 64%. That underlying performance matters. The quarter reflects continued growth and improving profitability across Legacy Seco together with a full quarter of Thermon and the early benefits of our strategic combinations. Total company orders were $778 million and we ended the quarter with approximately $2.2 billion of backlog. Our opportunity pipeline now exceeds $9 billion. Approximately 80% of our backlog relates to multi-industrial and energy applications, with approximately 20% related to data center applications. Importantly, the projects within that backlog are funded and actively progressing, rather than prospective projects that rely on future development activity to move forward. The thermon integration remains on track and ahead of schedule. We have now captured approximately $22 million of annualized net adjusted EBITDA savings, representing approximately 55% of the three-year target we laid out, and we've done so in the first six months. Those are annualized savings from

actions completed with benefits flowing directly into earnings over time. Organizational and cultural integration is progressing nicely as well, and the teams are increasingly unified and focused on executing together to serve our global customers. In the quarter, cash generation was another highlight. We generated approximately $154 million of adjusted free cash flow, bringing year-to-date adjusted free cash flow to $192 million. That cash generation supported debt reduction and brought quarter and net leverage to approximately two times. The combination of our backlog, pipeline, and integration progress gives us high confidence as we introduce our initial 2027 outlook. At the midpoint, we expect approximately $2.2 billion of revenue and $500 million of adjusted EBITDA. I will discuss the 2027 assumptions and ranges after Peter reviews our financials in more detail. Now please turn to slide number four. This slide puts the quarter and year-to-date into the context of the high-performance company we have built over several years. Since 2020, we have delivered sales growth at a compound annual growth rate above 20%, expanded EBITDA margins by more than 700 basis points, and we've completed more than a dozen accretive acquisitions. Our sales pipeline has expanded approximately six times and backlog has grown approximately tenfold. Those are powerful metrics that don't just happen by chance. It has been a steady series of focused investments and strong execution by our great teams. We have also broadened our portfolio. across industrial air, industrial water, energy and thermal management, we serve customers with different investment priorities and project schedules. That breadth provides opportunities across multiple markets, and each of our platforms have exciting growth opportunities heading into 2027. We recognize the questions that some investors are asking about the macro environment, including the durability of demand, The pace of infrastructure investment and the exposure of industrial suppliers to data center spending. Our view starts with the projects and customer relationships we manage directly. Our backlog consists of funded, permitted, and active projects. Cancellation, or often referred to as de-booking rates, remains very low and continue to track our long-term average of below one-half of 1%. Direct engagement with end customers gives us visibility into project requirements and execution schedules. We continue to monitor those schedules closely as projects move through engineering, procurement, and delivery. Backlog quality also supports our margin outlook. The booked margin profile provides a solid foundation for future profitability as projects convert to revenue. We then have Additional opportunities through sourcing, productivity, integration savings, and the operating benefits of higher volumes. The cash performance is equally relevant. Our model has relatively modest fixed cash requirements, excuse me, fixed capital requirements. And effective management of customer milestones and working capital can generate substantial cash. We saw that this quarter. The resulting debt reduction expands our capacity to support growth and future acquisitions. Additionally, we look at the combination of revenue growth and EBITDA margin as an indicator of performance. The combination of these two metrics is often associated with what's known as the Rule of 30 or Rule of 40 companies. These refer to companies whose numeric addition resulting from the combination of top-line growth rates and operating or EBITDA margins adds to over 30 or 40, as quite often those companies regularly receive higher trading multiples. On the basis shown in this deck, the combination for SECO is over 40, therefore a rule of 40 company for 2026. And our initial 27 outlook is to be a rule of 50 or higher company. So if premier industrial companies operate at a rule of 30 or higher, we are pleased to continue to be in this premier neighborhood. and finally on this slide we note that we have a track record of meeting or exceeding the initial annual guidance we provide and we continue to use the same planning discipline as we do each year. We evaluate customer demand, execution capacity and the risks in the operating environment and we translate all that into the opportunities and the challenges ahead. Now I will hand it over to Peter and he will walk through the quarter's financial results and our updated full year 2026 expectations. Peter? Good morning, everyone.

Peter Johansson | Chief Financial Officer:

Thank you for joining Todd, Marcio, and myself for a review of SECO's third quarter 2026 results and an outlook for the full year. Please turn to page six. On this slide, we present a summary of the key business metrics and performance highlights for the quarter. As a reminder, This is our first report with a full quarter of thermon in our reported results. And the resulting financial performance was outstanding, demonstrating both the continued strength of the legacy SECO businesses and the strong contributions from the thermon

acquisition. Revenue for the quarter exceeded $404 million, an increase of 105% from the prior year. Legacy SECO revenues increased 30%, supported by the accelerated conversion of our growing back loans. There were no material project delays that impacted our results in the quarter. Adjusted EBITDA for the quarter was $70.1 million, up 201% over prior year. resulting in a margin of 17.3%, 550 basis points higher than the same quarter in 2025. Legacy Seco adjusted EBITDA increased 64%. Adjusted earnings per share in the quarter was 60 cents, a 34 cent increase over the same period in 2025. Orders in the quarter were $778 million. higher by 234%, reflecting a book to bill of approximately 1.92 times. Legacy SECO orders increased approximately 165%. Quarter ending backlog reached approximately $2.2 billion, another record for SECO, with our legacy business backlog increasing by 167%. reflecting the continued strength and demand across our power generation, energy infrastructure, semiconductor, and broader industrial end markets. Another highlight in record in the quarter was our outstanding adjusted free cash flow, which reached $154 million. Conversion from adjusted EBITDA was outstanding, reflecting 220% conversion which allowed us to make substantial reductions in our gross bank debt balances resulting in a net leverage at quarter end of approximately 2.0 times, well within our target range. This result highlights the improved cash flow generation and margin profile of the new SECO portfolio that we fully expected would result from the combination with Thermon. For the first nine months of 2026, were slightly above $2 billion, exceeding full-year 2025 bookings by 90%. Revenue was $895 million, and the book-to-bill ratio was approximately 2.3 times. Year-to-date adjusted EBITDA was approximately $131 million, with an adjusted EBITDA margin of 14.6%. An increase of approximately 380 basis points over prior year. And through September, we generated $192 million of adjusted free cash flow. Strong collections and advanced payments from customers contributed to that performance. And we ended the quarter with approximately $530 million of net debt, a substantial reduction from the position at the end of the second quarter. Given the aforementioned orders and cash performance, we will be increasing our full year expectations for both metrics. We are maintaining our revenue and adjusted EBITDA ranges we raised in August. More to come on the full year 2026 outlook when we reach slide 10. Now please turn to slide number 7 for some additional details on our financial results for the third quarter and trailing 12 months. We concluded the quarter with a record backlog of $2.193 billion, up 205% versus prior year, and up 21% sequentially from our previous high of $1.82 billion. Backlog has now increased in 13 consecutive quarters and has been accelerating over the last eight quarters. Third quarter orders were $778 million. An increase of 234% over the prior year period, as our business platforms book significant orders across a wide range of end markets, including power generation, LNG and gas processing, natural gas transportation, semiconductor and electronics production, and industrial wastewater and produce water treatment. On a trailing 12-month basis, orders have reached $2.355 billion, a 147% increase over the prior trailing 12-month period, and book-to-bill was 2.12 times, an outstanding result. Revenue is another strong result in the third quarter, exceeding $400 million, 105% greater than last year, inclusive of a full quarter of Thurmond's performance. SECO's standalone revenue in the quarter was $256 million, approximately $21 million above the company's previously quarterly high set in quarter two of this year. We expect revenue growth to continue in the fourth quarter, tracking the significant expansion of our backlog and growth in orders, most notably in our power generation, semiconductor, and natural gas infrastructure applications. Trailing 12-month revenue finally broke through the $1 billion level, reaching $1.110 billion, a record for any 12-month period in company history of 55%. And we expect sequential revenue growth to continue, supported by our growing backlog, strong sales pipeline conversion, and demonstrated execution. Adjusted gross profit for the quarter and for the trailing 12 months increased 127% and 53% respectively on higher volumes and the benefits of the thermon combination. Sequentially, margins increased 262 basis points to 36.3%. This improvement was expected as margins moved higher due to improving volume and mix on larger projects, Newer Higher Margin Projects with Faster Revenue Recognition Profiles, Improving Execution and Operating Excellence Efforts, and the Benefits from Blending in the Thurmont Margin Profile. Trailing 12-month gross profit margins were 34.4%, a level we expect to maintain or deliver above. Adjusted EBITDA for the trailing 12-month period, which included four months of Thurmont operating results. was $160.4 million, resulting in a margin of 14.4%, an increase of nearly 336 basis points. Adjusted EBITDA delivery benefited from higher volumes, accretive thermon product margins, lower operating G&A expenses, ongoing complexity reduction efforts, including the benefits from our 80-20 effort, and lower corporate G&A spending. along with the higher adjusted EBITDA, free cash flow conversion was substantial. And I will

provide more color on cash flow on our debt position on slide nine. Please now turn to page eight for a few highlights on backlog. Backlog continues its impressive growth on both a sequential and year-over-year basis, closing the quarter at $2.193 billion. Book-to-bill in the third quarter was approximately 1.9 times. Our backlog, which is all firm and confirmed with customer POs and recovery terms in the rare case of a cancellation, reflects a substantial portion of our future revenue and has now increased by approximately 10.2 times since the end of 2021. Our sustained strong order performance and our continued success in converting our nine plus billion dollar sales opportunity pipeline underpins our expectation of extending the trend of greater than 25% top-line growth for the full year in 2026. In terms of backlog composition, power generation projects for customers in utility, both gas and nuclear powered, industrial heat and power, and data center applications represents approximately 60% of our quarter-ending backlog. The remaining approximately 40%, consists of a diverse mixture of projects and customers across energy and industrial end markets, including semiconductor and electronics, natural gas processing and transport, hydrocarbon and chemical processing, process electrification, and industrial water and wastewater treatment. The legacy thermon business represented approximately 13% of SECO's backlog. as the Thermon revenue mix is comprised of shorter cycle and faster turning orders and projects. Now please turn with me to slide nine for an update on cash flow and indebtedness. Third quarter adjusted free cash flow continued the strong momentum started in the second quarter as we generated approximately $154 million of cash and pushed our year-to-date adjusted free cash flow to approximately $192 million. An increase of approximately $191 million year-over-year, representing approximately 147% of adjusted EBITDA. For the trailing 12 months, pre-cash flow generation slightly exceeded $200 million, or approximately 125% of adjusted EBITDA. Cash flow generation benefited from strong collections in the quarter on second quarter billings for large project milestones, receipt of down payments for new bookings, growth in our build and excess balances, and improved working capital management with a strong and increasing focus on inventory. Numerous major project milestones and the resulting customer billings were realized in the third quarter, creating customer receivables that we expect to collect during the fourth quarter and first quarter of 2027, continuing our free cash flow generation surge. Capital expenditures in the quarter were modest and largely driven by our ongoing ERP migration and consolidation initiative, which we expect will be essentially complete for SECO legacy entities by mid-2027. And we spent money on select projects in acquired facilities that were ongoing within the thermon businesses. With the MODX CAPEC needs and our strong cash generation, we were able to apply a majority of our cash flow to reduce our debt balance. Gross debt at the end of the third quarter of approximately $604 million was lower by approximately $128 million, reducing our net debt to approximately $530 million and a third quarter and leverage ratio of 2.0 times our trailing 12-month bank EBITDA. This is at the low end of our targeted leverage range of 2.0 to 2.5 times, demonstrating once again our ability to quickly reduce the level of our borrowings made to support a creative and strategic growth initiatives. With the debt repayments we have made in the quarter, SECO has created substantial capacity of approximately $344 million within our current credit facilities, providing substantial liquidity to support our anticipated working capital, trade finance, capital expenditure, and strategic investment requirements. And with additional sizable collections expected in the fourth quarter, Supporting further repayments, we anticipate year-end leverage to be further reduced below the low end of our target leverage range, further increasing our revolver capacity and further lowering our cash interest expenses. Now let's flip to page 10 for an update on our full year 2026 outlook. We are increasing our full-year orders outlook to $2.5 billion or greater as market demand remains robust and our sales opportunity pipeline continues to expand. On this level of orders, we expect year-end backlog to exceed $2.2 billion. We are also raising our adjusted free cash flow outlook to approximately 100% of adjusted EBITDA. and increase from our previous expectation of at least 55%. This improvement reflects the cash already generated year to date and our current expectation for further collections and project working capital improvements through two years end. In August of this year, we increased our outlook for full year revenue and adjusted EBITDA, incorporating the impact of the Thermon acquisition and expected higher SECO legacy business growth. We are maintaining our August revenue guidance of $1.3 billion to $1.375 billion and adjusted EBITDA of $200 to $225 million. The adjusted EBITDA outlook includes approximately $5 million of thermon cost synergies that will be realized during 2026, and as a reminder, includes seven months of thermon results beginning from June 1st. On a pro forma calendar year basis, including a full year of Thurmond results, we expect that 2026 revenue would reach $1.5 billion to $1.6 billion, an adjusted EBITDA

of $255 million to $280 million. That pro forma perspective provides a better jumping off point for comparing the 2027 outlook that Todd will share with you shortly. And that concludes my review of SECO's third quarter 2026 results and a discussion of the full year outlook. I will now pass the mic back to Todd to provide, as we have in prior years, our initial view of next year's outlook and his closing remarks.

Todd Gleason | Chairman and Chief Executive Officer:

Thanks, Peter. Please turn to slide number 12. As Peter just mentioned, each of the past five years on our third quarter earnings call and release, We provide an additional outlook for the next fiscal year. In each year, we substantially go through a similar process to compile this initial outlook. We provide our guidance construction roadmap on this slide. Our initial 2027 outlook reflects the ongoing business we can see through customer engagement, our order book, and the execution plans associated with our operating teams and their goals and objectives. We start with an assessment of our sales pipeline, which has risen to above $9 billion. We combine that pipeline analysis with a similar evaluation of our backlog, which, as you know, is approximately $2.2 billion. Power generation markets remain very strong and our diversified industrial businesses provide additional opportunities. We expect growth across all of our business platforms as we head into next year. The margin profile of Backlog also supports this outlook. Thermon adds to the profitability of the combined portfolio, while productivity, sourcing, and operating execution provide further upside. Those benefits are reflected in our planning. Integration savings are progressing ahead of schedule. As I noted earlier, we have captured over $20 million of annualized net adjusted EBITDA savings. which is approximately 55% of our three-year target. We now expect to capture approximately 70% or more of the target by the first anniversary of the acquisition. Our teams have also actioned approximately $2.5 million of revenue synergies. The opportunities include thermal solutions on power generation and gas filtration projects, along with early opportunities in international water applications. We continue to see the potential to add one or two percentage points to Thermon's organic growth through commercial synergies. In just a few months since integrating Thermon, we are off to a solid start. We are balancing those opportunities against uncertainty in the operating environment. Inflation, policy changes following the election, geopolitical developments, and sentiment around AI and data center investment all warrant attention. We've considered those factors in constructing our outlook. Some factors will improve the market while others might create more pressure or uncertainty. That said, our leadership team has the experience and we have processes in place to monitor and adjust. I would remind our audience that since initiating our annual guidance process in the third quarter of 2021 for full year 2022, We have exceeded our initial guidance in four of the five years and essentially met it in the remaining year. The average outperformance has exceeded 10% for revenue and adjusted EBITDA. That history reflects our planning processes and execution. While our current ranges reflect the information that is available today, we remain very confident in how we build our outlook. Please turn to slide 13. It is rewarding and exciting to provide our 2027 outlook. At the midpoint of our initial 2027 guidance, we expect approximately $500 million of adjusted EBITDA on approximately $2.2 billion of revenue. That implies adjusted EBITDA margin of approximately 22.7%. Just tremendous growth and year-over-year performance on almost every metric. The progression reflects our full year of Thermon, the conversion of our larger backlog, and the margin and cost opportunities across the combined companies. We have direct customer engagement supporting the projects in that backlog, and the data center projects, which I already mentioned represent about 20% of our backlog, are all progressing on schedule. The slide also provides a preliminary view of continued growth in 2028. We provide this preliminary growth projection based on meaningful discussions we have with customers and our long-term analysis of our opportunity pipeline, which we anticipate to grow above $10 billion in the next few quarters. With these inputs, we currently see preliminary 2028 delivering double-digit top-line and bottom-line growth. This would yield adjusted EBITDA margins in that period of approximately 23.5%. We hope this snapshot of 2028 helps provide insights into our current assessment of market opportunities ahead, not just in 2027. While there is much to do, we look forward to and are confident in our ability to execute through the upcoming periods. As always, these operating plans include appropriate cost actions and contingencies alongside the benefits of integration and productivity. We will update our expectations as the year progresses and Our visibility develops. Turning to

slide 14, this simply provides our 2027 outlook with a slightly different format in more detail. Just to repeat a few things, as I just mentioned, our 2027 revenue outlook is for $2.1 billion to $2.3 billion, and we expect adjusted EBITDA of between $475 and $525 million. At the midpoint, revenue growth exceeds 60% against the 2026 reported outlook and is up approximately 40% against the pro forma outlook. Adjusted EBITDA growth exceeds 130% against the reported outlook and would be up approximately 90% against the pro forma outlook. Again, just tremendous growth. We expect orders to grow 20% or more with a strong book to bill ratio throughout the year. Our pipeline and market activity support that execution, while backlog provides visibility to revenue. The EBITDA outlook incorporates higher backlog margins, integration savings, and the operating benefits of volume and productivity. It also factors in appropriate levels of inflation and other headwinds. We expect adjusted free cash flow conversion in the range of 50% to 60% of adjusted EBITDA. This initial assumption reflects our multi-year average. We will continue working and other capital programs to pursue additional cash generation as project schedules and customer terms allow. Now please turn to our final slide, 15. Seco serves diverse industrial and environmental markets, and we see growth opportunities across more than a dozen business platforms. Our third quarter performance reflects the investments we have made in our people, our processes and systems, and together with the value of the Thermon combination and their great teams. The third quarter builds upon our strong legacy of Secor growth. A full quarter of Thermon and substantial cash generation are also highlights. Integration is ahead of schedule and backlog and pipeline support our initial 2027 outlook. Our leadership teams remain focused on customer execution and the operating actions that are within our control. We continue to monitor market developments and we'll adjust where necessary and communicate our progress. Once again, and as always, I thank our global teams for the work that is done to produce these incredible results. And thank you to our customers and shareholders for your continued support. With that, operator, I'd like to open the line for questions.

Conference Operator | Operator:

Thank you. As a reminder, to ask a question, please press star 11 on your telephone and wait for your name to be announced. To withdraw your question, please press star 11 again. Our first question comes from the line of Aaron Spichella with Craig Hallam Capital Group. Your line is now open.

Aaron Spychalla | Analyst, Craig-Hallum Capital Group:

Yeah, good morning, Todd and Peter and Marcio. Thanks for taking the questions. You know, appreciate all the color on everything and including data centers. You know, maybe first question on backlog. I mean, it sounds like most of your backlog and growth is coming from PowerGen and other areas of the industrial complex. Can you just talk about the margins within that backlog and how much conversion you're expecting in 2027 guidance and how that maybe compares to prior years?

Todd Gleason | Chairman and Chief Executive Officer:

Yeah, I think a lot of consistency in how it compares to prior years. Things can move up and down a little, as always. But to stay true to that, we expect at least 70% to convert in 2027 in our current backlog. So as we wrap up the year, as backlog grows and we enter 2027, that ending 2026 backlog will turn at least 70%, sometimes higher, in the next year. So that's usually our average. Daniel Berryman, Peter Kurt Johansson, Alyson Gregory Richter, Candace Harris-Peterson, Mary Rusnak, Todd Gleason We are at a higher gross margin level in backlog than our current gross margins that we just reflected in year-to-date and in the quarter. So we have a lot of visibility to our ability to execute on the margin profile that we've outlined. I'd say that as we book projects here in the third quarter and we look at the projects that we expect to book in the next few quarters, we like the margin profiles associated with those as well. So while there are areas around inflation and supply chain constraints that we monitor and we constantly are ensuring that we are addressing, we really like the way that our revenue is going to turn next year. It's very much in line with our expectation.

and as I just suggested, the margins are certainly higher than what we've delivered already.

Aaron Spychalla | Analyst, Craig-Hallum Capital Group:

Understood, thanks. And then maybe on the pipeline and the orders in the corridor, any areas of strength to note for the corridor orders? And then I think I heard commentary of the pipeline growing to $10 billion. Just maybe talk about You know, what's driving that? And again, just conversations with customers that you're having on kind of interest rates and inflation.

Todd Gleason | Chairman and Chief Executive Officer:

Yeah, so what's driving the $10 billion preliminary view of where it's heading is, you know, our sales pipeline, the $9 billion, are projects that we know will be, we anticipate will be actively won or lost or, you know, Daniel Berryman, Peter Kurt Johansson, Mary Rusnak, Todd Gleason and many more. People that track us. We continue to grow in new markets, geographies. Those markets and geographies in the industrial space are quite often growing. So, you know, us growing our sales pipeline is simply a result of the team's efforts to introduce our services and solutions to new vertical markets and new geographic markets. I know Peter and I spend a lot of time on our operating reviews with the businesses talking about the growth of their markets and pursuits. And that has typically been one of our healthiest areas of strategic focus organically is expanding our opportunity set, our at-bats, as they say, in the various vertical markets and geographic markets. And we don't see that slowing down anytime soon.

Aaron Spychalla | Analyst, Craig-Hallum Capital Group:

Great. Thanks for taking the questions. I'll turn it over.

Conference Operator | Operator:

Thank you. Our next question comes from the line of Bobby Brooks with Northland Capital Markets. Your line is now open.

Tomohiko Sano | Analyst, J.P. Morgan:

Hey, Bobby. Good morning.

Peter Johansson | Chief Financial Officer:

Bobby, you're breaking up. Can you start over? We didn't hear any of your questions.

Bobby Brooks | Analyst, Northland Capital Markets:

Hey, can you guys hear me better now?

Todd Gleason | Chairman and Chief Executive Officer:

Yes, thank you.

Bobby Brooks | Analyst, Northland Capital Markets:

Sorry about that. So when you guys initially bought Thermon, it was discussed how given how earlier SECO gets involved in certain projects, it's given, you know, several months to even a year ahead of when Thermon's team might have known about certain projects that need their thermal management. It seems like, I think you mentioned there were some sales synergies in the quarter that were captured. Is that related to that? And just wanted to just get a broader update of like, is that still something you think can really help, you know, add organic growth to the business and just help cross-selling?

Todd Gleason | Chairman and Chief Executive Officer:

Yeah. I'll start and then Peter can add. He's also done a lot of work on this. So the way your question was worded is accurate. Our visibility to the sales pipeline and our backlog gives a unique access point for Thermon and their to go and evaluate opportunities to cross-sell or sell into those projects or those upcoming projects. So that visibility is a salesperson's dream. And we provide, therefore, access to new market pursuits for Thermon every day across all of our platforms. The sales to date reflect some of that. Where we have already booked or will be booking a project in backlog, we see an opportunity to include a heat process solution, an immersion heater, a heat trace, or something similar, and we get those thermon teams involved, and we get them qualified on the project, and off we go. So that's what's been happening there. There's a lot of other opportunities, I think, for both sides. Thank you for joining us. with conviction that we believe Thermon will, the Thermon business has at least a point of organic growth as a result of this combination. And I would say that there's additional sales on the Seco side as well that can add just nice growth to the combination.

Peter Johansson | Chief Financial Officer:

Bobby, you used the term called cross-selling. While that is not the strategy for bringing the commercial teams together, it is in some instances what we're finding happens is that one of our teams passes a lead to another team and they close. We are not creating a single sales force with an organization that sells across all of the applications and technologies. We're still maintaining the integrity and the focus of our business platforms because that's what our customers expect and that's how our teams best execute. Where we're seeing the benefits are where customers are asking us to present them the solution with more technology in the package. So we need to be careful that when you use the term cross-selling, we're not seeking the synergies of one guy selling everything. That's just not our strategy.

Bobby Brooks | Analyst, Northland Capital Markets:

Thank you for that color, Peter. That's very, very helpful to think of. And then just on to kind of piggyback on Aaron's question a little bit more so, I think you mentioned 70% of the 20, 70% of what will exit the back or 70% of the year-end backlog expected to convert into sales in the next 12 months. Could you just discuss so then like the remaining bridge of the 27 guide is just like typical cadence of like more short cycle book and bill stuff and am I thinking of that right or is there a little more nuance?

Todd Gleason | Chairman and Chief Executive Officer:

Daniel Berryman, Peter Kurt Johansson, Alyson Gregory Richter, Candace Harris-Peterson, Mary Rusnak, Todd Gleason Thank you for joining us. I don't know what percentage of companies do that in late October or early November, but we are certainly in the minority of companies that provide next year's outlook this early. But that visibility that we have in backlog and in our sales pipeline is help support that confidence. And it's not just confidence. It really supports a bottoms-up model that allows us to see 70% of our revenue walking into the year almost with high visibility. And then the other 30 or so percent of our revenue is what most companies do, which is we model the market. We model our typical demand. We model our flow of our short cycle sales and aftermarket and services. So It's a combination of visibility and knowledge of how our markets are growing and how we're benefiting from those markets.

Bobby Brooks | Analyst, Northland Capital Markets:

Super helpful. And just last one for me. I know in the past there's been some excitement around large industrial water projects, specifically within the Middle East, kind of tied to some new energy production over there. I was just curious, was any of the 3Q orders benefit from that? Has that opportunity changed just with continued kinetic energy over there? Just wanted to get a sense of what's happening over there.

Todd Gleason | Chairman and Chief Executive Officer:

Yeah, water has had good growth in the quarter. We have very large opportunities that we spoke of earlier this year, and we still have those opportunities. Some of those have been a little bit delayed because of some of the conflicts in the region, in the Middle East region, and so we're We're still seeing there's a large appetite for those when that disruption subsides. We don't have that. We haven't put that in our outlook so much. We talk about it, and they're still there. They're included in our pipeline. But at this point, we remain very confident in our double-digit, strong double-digit growth across industrial water. And those larger-scale projects will be upside when they happen.

Bobby Brooks | Analyst, Northland Capital Markets:

Terrific to hear. Congrats on a strong quarter again, guys. I'll return to the queue.

Todd Gleason | Chairman and Chief Executive Officer:

Thanks, Bobby.

Conference Operator | Operator:

Thank you. Our next question comes from the line of Rob Brown with Lake Street. Your line is now open.

Rob Brown | Analyst, Lake Street:

Good morning. Just wanted to maybe hit the visibility question again, kind of looking into 28. On the power side, how much visibility do you typically have as these power projects get developed? I assume you sort of, you know, I guess know by several years out that things are happening, but just maybe talk about the visibility in the power market in particular and how much kind of visibility you have there.

Todd Gleason | Chairman and Chief Executive Officer:

A lot of visibility, Rob. You know, this is probably the market we have the most visibility at the moment. You don't have to look much further than a lot of the power generation reports that are out there, both public companies reports that are out there that are selling power generation solutions, as well as utility and demand, the need for more power for a range of electrification, digitization, compute, grid, baseload power. There is no shortage of a need for power. It is not just tied to one thing. I think that themes that are often associated with it in the short term are certainly important themes and important markets, but they're not the only ones. And so even if some of these markets adjust somewhat in terms of their attractiveness, the need for power doesn't seem to be modulating much. And as a result, we see power markets out three, four, five years. and you know we're not we're not here to to make a claim that you know we're going to win x percent of the jobs etc but as a result of the need for power and infrastructure across energy to support the need for power gas infrastructure and other related energy transition markets we would say our visibility is probably at the highest it's been for a two three or four year cycle and this is the first time that we've sort of given 2020, you know, the next year's outlook with a preliminary sort of snapshot of the following year. But we thought if there was ever a time to help the investment community with our view, our informed and deeply in sort of an educated view of the markets that we serve and are a leader in, that we see strength in those key markets, especially power generation markets for several years. And I guess I said, it is not just based on one thing. It is based on a multitude of growth Thanks for that color.

Rob Brown | Analyst, Lake Street:

And then on the EBITDA margin, you're kind of getting consistently into the low 20%. What sort of you're thinking on where that EBITDA margin can sustain at or what's your sort of goal in that EBITDA margin level?

Todd Gleason | Chairman and Chief Executive Officer:

Well, we certainly want to sustain EBITDA margins, and we have a track record of doing so. It feels good to use the number 20-something associated with EBITDA margins. Daniel Berryman, Peter Kurt Johansson, Alyson Gregory Richter, Candace Harris-Peterson, Mary Rusnak, Todd Gleason We're pretty committed to that. We're going to continue to look at ways to get productivity. We're just getting started on a lot of our operating excellence journeys as a combined company with us and Thermon. Anything we do going forward we feel will benefit from our maturity in these processes and programs. Volume leverage is always going to be attractive for us when we get up to these levels. We've got a ton of growth in front of us. I don't know that I'm ready to start to talk about margins in a long-term range above this 22%, 23%, but I can assure you that as we think about a longer-term outlook and guidance, which we'll be doing at some point in 2027, they will be higher.

Peter Johansson | Chief Financial Officer:

Rob, think about it this way. Rule of 40 company, 20 and 20, for a sustained period with higher rates of cash conversions. and a very deep pipeline of opportunities to invest that additional free cash flow for growth. I'm not sure whether you're 22% or 24%. It makes much of a difference. Once you've cleared the 20% hurdle and are growing 20% top line and have the number of and the track record of converting cash into growth as a compounder, you need to say much more.

Rob Brown | Analyst, Lake Street:

Okay, yeah, perfect. Great. Thank you. Congrats on all the progress. I'll turn it over.

Conference Operator | Operator:

Thank you. Our next question comes from the line of Tomohiko Sano with JP Morgan. Your line is now open.

Tomohiko Sano | Analyst, J.P. Morgan:

Hi, good morning, everyone.

Peter Johansson | Chief Financial Officer:

Hello, Tomo.

Tomohiko Sano | Analyst, J.P. Morgan:

Thank you. First, congratulations on a very strong quarters. My question is on 2027 and 2020 outlook. What is the most likely constraints to deliver this outlook, including capacities and labor supply chains or working capital? And then what levels of investment will be needed to address it? Thank you.

Todd Gleason | Chairman and Chief Executive Officer:

Thanks. Good question. Always a very appropriate question when we deliver preliminary outlook. And you could ask that question in 21. You could have asked that question in 2022. You could have asked that question in 2023. I think you get my point here. We view the same constraints. Each year there's usually a unique one, let's just say. It could be back in the day, it could be a unique constraint that we certainly can't control like COVID, Daniel Berryman, Peter Kurt Johansson, Marcio Pinto, Mary Rusnak, Todd Gleason have been in our jobs long enough to know there are going to be some things that come up in 27 and 28 that we just can't predict today. And, you know, you want operating teams, you want a team with a lot of visibility in their projects, in the relationship with the direct end customer that can then go, okay, well, how do we navigate and adjust for that uncertainty? So, you know, every time we give guidance, Tomo, and to the broader audience, we think about what could go wrong first, right? We think about what are the challenges? Inflation, could that go higher? What does that look like? Can we price it through? Will we get productivity? What could be coming around the next corner that we just can't anticipate? Maybe it's another domestic situation that we have to understand or an international situation. Those things you can't predict, but you have the experience built into your processes to react appropriately and if not even proactively. As far as the things we do know, you know, look, I think that we feel very good about our supply chains. We feel very good about the current cost environment and inflation environment. We have a great group of teams and we're growing. We're adding talent regularly. That is, you know, not getting easier, but we have our arms around it. So I think that we feel very balanced as we do each year. that there's more opportunities to exceed. There are challenges that we know, and we have our arms around those, and we have them priced in. And then we have challenges that we don't yet know, but we have the experience and the processes to absorb them and adjust. And that's our expectation. Again, our track record is proven. Our processes are proven. And I don't think we're doing anything particularly different here this year as we constructed our 27 outlook.

Tomohiko Sano | Analyst, J.P. Morgan:

Thank you. That's helpful. And on the other one is the balance sheet and capital locations. So the net leverage has fallen by 0.7 turns to 2.0 times since the Salmon acquisition closed. What is your target leverage and how will you prioritize incremental cash amongst the debt reductions in BestBend and M&A? Thank you.

Todd Gleason | Chairman and Chief Executive Officer:

We're going to invest and grow. That's what we do. Daniel Berryman, Peter Kurt Johansson, Alyson Gregory Richter, Candace Harris-Peterson, Mary Rusnak, Todd Gleason Interest rates are at a little bit of a higher level, so if you can't generate free cash flow and pay down your debts, you should be thinking about investments differently, but we can, and we're going to think about investments for growth, I think, appropriately, and therefore aggressively. We're both a programmatic investor in growth. internally for organic growth. We have built teams around the world. We have built supply chains around the world. We are innovative in our application engineering and for solutions. And we also then invest programmatically around M&A. We buy leading, winning companies with great teams, cultures, and operating environments. We add their niche industrial leadership to SECO's portfolio, and we help each other grow even more. So how we use our balance sheet internally will be for growth. How we use our balance sheet, you know, for inorganic will be M&A, and we will continue that programmatically for years to come.

Tomohiko Sano | Analyst, J.P. Morgan:

Awesome. Thank you very much. Congrats again.

Conference Operator | Operator:

Thank you. Thank you. Our next question comes from the line of Jim Ricciuti with Needham & Company. Your line is now open.

Jim Ricchiuti | Analyst, Needham & Company:

Thanks. Good morning. Hopefully, you can hear me okay?

Conference Operator | Operator:

We can. Yeah.

Jim Ricchiuti | Analyst, Needham & Company:

Good morning. Perfect. Morning. I'm just wondering, just with respect to the last comment on M&A, I'm wondering, are the opportunities you're evaluating, first of all, how active is the pipeline, just given the way you're paid down debt and with the cash flow generation, but are the opportunities you're evaluating changing at all in light of either, you know, the market conditions or the changing macro environments?

Todd Gleason | Chairman and Chief Executive Officer:

We continue to see incredible opportunities, Jim. We have built an extremely robust pipeline of M&A. It allows us to move swiftly towards the best candidates for acquisition, and we then focus on Thank you for joining us. We continue to grow and achieve success together post-integration. And I think that the businesses that we're finding that are out there across industrial niche leadership areas continue to be very attractive. And any acquisition we do I think will fit our profile very nicely, and we feel good about the pipeline.

Jim Ricchiuti | Analyst, Needham & Company:

Good. Follow-up question just on that. The initial 27 outlook that you're providing today, and thank you, by the way, for all the color, not only 27, but even looking out to 28. Curious, I think you said in the deck, high single-digit growth within the thermon business. You talked about another couple of points of growth. Is that baked into the initial 27 guide? And then just you also alluded to pricing. And I'm just wondering how the overall pricing environment across the portfolio stands as it relates to that initial 27 outlook. So kind of a two pronger for 27.

Todd Gleason | Chairman and Chief Executive Officer:

I'll start with price. Price remains good. We look at price a little different maybe than some companies because so much of what we do is project by project, so it's not your standard list price. We do have at least 35% of our company is standard product of some sort, so they have a standard list price of which we've done a nice job of increasing to keep up, if not get ahead of inflation and the pressures associated with that. And look, it's really a strong demand environment across reshoring. It's a strong demand environment across infrastructure. It's a strong demand environment in power and in energy. So look, we're in a good environment for our ability to, if we're executing, we're getting price and we're going to be able to defend it. and then yeah on the Thermon you know they grew at double digits in the third quarter which is very very strong for them from a historic perspective. I think Thermon can keep that up. They have incredible leadership. Their organization is focused on the markets that they can see with the best growth. We're putting in probably high single digit for now but there's upside in Thermon not just Thank you. Thanks, Jim.

Conference Operator | Operator:

Our next question comes from the line of Joseph Giordano with TD Cowen. Your line is now open.

Chris | Analyst, TD Cowen (on behalf of Joe Giordano):

Hi, good morning. This is Chris on for Joe. The midpoint implying a 22.7% EBITDA margin. Just wondering if you could talk about what changes support reaching that level sooner than the prior expectation for approximately 20% from the June framework. and should we expect margins to approach the 2027 midpoint earlier in the year or is the outlook dependent on a meaningful second half ramp?

Todd Gleason | Chairman and Chief Executive Officer:

Yeah look it's a gradual build I'd say a little bit as we get volumes higher because some of it is related to volume absorption in a good way so the you know margin expansion of you know of you know, associated with volumes grow throughout the year a little bit. That's just, you know, the way we're currently building it. I think you're, you know, from where we're at today in the third quarter, you're going to continue to see EBITDA margin expansion and, you know, but so, you know, a little bit more in the second half than the first half to

answer the question, Chris. We appreciate that you guys are going to try to want to model that in accurately. So, you know, obviously we can be helpful in how to think about how volumes look like they could grow throughout the year based on our Based on our project portfolio, et cetera. But to get above 20% a little faster, it's all reflected in this higher growth, this higher growth profile. And the margins that we have in our backlog associated with Jim Rusciutti's question on pricing and just really good demand cycle, it's all reflected in our backlog margin, which allows us to be a little ahead of schedule.

Chris | Analyst, TD Cowen (on behalf of Joe Giordano):

Great, thank you. And should we expect normal seasonality in the first quarter of next year, or does the size and timing of backlog conversion create a meaningfully different start to the year?

Todd Gleason | Chairman and Chief Executive Officer:

Yeah, I'd expect a similar seasonality to the first quarter. Some of it's seasonal, you know, just coming Coming into the year, a lot of projects reflect that. A smaller quarter, in a sense, you know, and a bit of a reset on project timing and similar nature. So, look, you know, we don't have anti-gravity issues as we walk into 2027 on some of those seasonal components. And I would just suggest that, you know, that it's going to be somewhat similar to our typical build where Q1 is one of our lowest, if not the lowest quarters, just in terms of size and volume, etc., We also have some Q1 expense and cash payments associated with everything from taxes and other beginning of year bonuses and similar to that. So again, there's just some seasonal factors in the market. There's some seasonal factors on our P&L, and there's some seasonal factors that are just, you know, they're very consistent.

Chris | Analyst, TD Cowen (on behalf of Joe Giordano):

Great. Thank you very much.

Todd Gleason | Chairman and Chief Executive Officer:

Thank you.

Conference Operator | Operator:

Thank you. And I'm currently showing no further questions at this time. I'd now like to hand the call back over to Todd Gleason for closing remarks.

Todd Gleason | Chairman and Chief Executive Officer:

Okay. Thank you. And thanks for everyone for the questions. I know we went a little over today. Thank you for joining us today. continue to deliver for our customers every day. And as always, I'm proud to lead SECO as we protect people, we protect the environment, we protect our customers' investment in their industrial equipment. We look forward to providing more updates as we go through the next few months and as we head into 27. Have a great rest of your day, and we'll talk to you soon. Thank you.

Conference Operator | Operator:

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