

NYSE:THR Q2 2025 Earnings Call Transcript

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Operator | Conference Operator:

Greetings and welcome to Thermon Group Holding Inc's earnings call for the second quarter 2025. At this time, all participants are on a listen-only mode. A question and answer session will follow the formal presentation. If anyone requires operator assistance during the conference, please press star zero on your telephone keypad. As a reminder, this conference is being recorded. It is now my pleasure to introduce your host, Yvonne Salem, Vice President, FP&A and IR, thank you. You may begin.

Yvonne Salem | Vice President, FP&A and Investor Relations:

Good morning, and thank you for joining Thermal Group's Fiscal 2025 Second Quarter Results Conference Call. Leading the call today are CEO Bruce Sainz and Chief Financial Officer Dan Schott. Earlier this morning, we issued an earnings press release, which has been filed with the SEC on Form 8K, and it's also available on the next relations section of our website. Additionally, the slides for this conference call can be found in our IR website under News and Events, IR Calendar, Earnings Conference Call, Q2 2025. During the call, we will discuss some items that do not conform to generally accepted accounting principles. We have reconciled those items to the most comparable gap measures in the tables at the end of the Earnings Press Release. These non-GAAP measures should be considered in addition to and not as a substitute of measures of financial performance reported in accordance with GAAP. I would like to remind you that during this call, we might make certain forward-looking statements regarding our company. Please refer to our annual report and most recently quarterly report filed with the SEC for more information regarding our forward-looking statements, including the risks and uncertainties that could impact our future results. Our actual results might differ materially from those contemplated by these forward-looking statements, and we undertake no obligation to publicly update any forward-looking statements, whether as a result of new information, future developments, or otherwise, except as might be required by law. Today's call will begin with remarks from our CEO, Bruce Baines, who will provide a review of our recent business performance. including an update on the progress we have made on our strategic initiatives, followed by a financial update and review of our CFO, John Schott. Bruce will then wrap up our prepared remarks with an update on our business outlook. At the conclusion of these prepared remarks, we will open the line for questions. With that, I'll turn the call over to Bruce.

Bruce Sainz | Chief Executive Officer:

Well, thank you, Yvonne, and good morning to everyone joining us on the call today. Before I begin my comments, I'd first like to start by welcoming our new Chief Financial Officer, Jan Schott. Jan is a proven public company finance executive who brings significant financial expertise and deep capital markets experience to Thermod. We're very excited and fortunate to have her joining our team. Jan, welcome aboard. I and the rest of the management team are looking forward to working with you. Turning now to slide three. During the second quarter, we remained laser focused on executing against our strategic priorities, highlighted by improved bookings momentum, further progress on our operational excellence initiatives, and another quarter of financial discipline leading to strong free cash flow generation. In addition, we executed against our stated capital allocation priorities with the acquisition of FOTI and the return of capital through our share repurchase program. I think it's important to highlight that while we continue to effectively manage costs to the current level of demand, we've not wavered on our capital allocation to advance strategic initiatives while augmenting our organic growth. Since the start of the calendar year, we've acquired vapor

power, which increased our exposure to more diverse end markets and electrification. This integration is going well, and we're pleased with the strong level of market demand that we're seeing for these products. Just last month, we announced the acquisition of Fati, significantly expanding our geographic footprint in the Eastern Hemisphere. In spite of some short-term weakness in capital spending, we have continued to invest in our organic growth initiatives to further strengthen our competitive positioning over the long term. So with that, I'd like to turn to the second quarter, starting on slide four. We were very pleased with the improved order momentum we're experiencing during the second quarter, with orders up nearly 13% on a reported basis and 3% excluding the benefit from vapor power, resulting in an organic look-to-bill of almost 1.17 times. The strength was generally broad-based, and while we're still seeing extended decision cycles, and some uncertainty from customers, primarily on larger capital projects, we are encouraged by the growing opportunities pipeline and improved order momentum. As a result of the improved order trends, our quarter-ending backlog increased 29% on a reported basis and was up 3% organically. The timing of our backlog remains somewhat extended with many of the project wins currently in engineering with execution planned in fiscal 2026, which is a positive trend going forward. After generating 23% year-over-year organic growth in a record FY24Q2, our revenues declined by 7.4% year-over-year, which was in line with our expectations as the contribution from vapor power and stability from our materials revenue were offset by continued weakness in large project revenues and the timing of revenue recognition. Excluding vapor power, our revenues declined roughly 17% on an organic basis, driven by a 51% decline in our large project revenue during the quarter. Our short cycle OPEX revenues, which consist of our materials revenues and small project business, remained a stabilizing force during the second quarter, with revenues down only modestly as customers continue to focus on maintenance and repair spending. This balance in our model is a function of our focus on diversifying our in-market exposure and growing our installed base of customers. The result is a more resilient and stable revenue base through the cycle. As we detail on slide five, our materials and small project revenues represent over 80% of our revenues on a trailing 12-month basis, while our large project revenues were only 20% of the total. Our current mix provides a more stable and predictable revenue stream, as well as a more profitable mix, given our OPEX revenues consistently generate higher gross margins. Our OPEX revenues have grown nearly 11% on a TTM basis and have increased over 1% organically, while our large project revenue has declined 20%. The growth in our OpEx revenue, despite the uneven demand environment over the last several quarters, highlights the benefit of our deep installed base and recurring revenue exposure. Another key aspect of our strategy you've heard me discuss has been our goal to reduce exposure to the oil and gas sector. As I discussed last quarter, we have achieved our fiscal year 26 goal of generating at least 70 percent of revenues from diversified in markets. We remain committed to maintaining or further improving this metric, and while we did see a slight rebound in oil and gas bookings during our Q2, we still generated just over 70% of orders from diversified end markets during the period. It's important to note that we're not moving away from large projects, and large projects will always be an important driver of our business to enable growing the installed base. We have begun to see some signs of movement in large capital projects this quarter. In fact, we secured a large multi-year transit order in excess of \$8 million driven by infrastructure investments and a large Canadian carbon capture polyethylene unit valued at over \$8 million as well. Our pipeline of sales opportunities has now grown to over \$1.2 billion and with roughly 320 million in decarbonization opportunities, and we believe that we are well-positioned to benefit as large project spending trends improve. We don't believe there are any longer-term factors driving the recent project weakness. With the elections behind us, we're optimistic that sales cycles will start to normalize as customers gain more clarity moving forward. Turning now to slide six and our strategic pillars. Since I've already given you some color on our installed base and our diversification efforts, I'd like to take a moment to update you on our most recent acquisition, followed by an example of a nice energy transition market opportunity we're seeing. Turning now to slide seven. On October 2nd, we completed the acquisition of FATI, an industrial heater business based in Milan, Italy. FATI has a 79-year history a list of loyal customers, and is a very well-respected brand for high-quality heaters and demanding industrial applications. Their certifications and customer approvals are key in accelerating our ability to serve growing markets for electrification and decarbonization in Europe and across the Eastern Hemisphere. Revenues on a trailing 12 basis were roughly \$13 million. The business is also experiencing strong demand growth and they currently have a backlog in excess of 15 million with a robust pipeline of incoming opportunities. The purchase price of 12.5 million euro

is roughly equivalent to one year of sales. We're excited to welcome the Fatih team to Thermon and are already engaged to drive operational improvements to increase capacity to grow the business while expanding operating margins. Turning now to slide eight. As various technologies compete to provide a more sustainable energy future and electrification and data centers are driving increased electricity demand, we're seeing nuclear reemerge as a key piece of the future low carbon energy mix. Historically, Thermon has supplied heaters and filtration systems to the nuclear market through our CalorieTech heater line and 3L filtration systems. Base loaded power generation stations are now required to operate more flexibly with frequent shutdowns and restarts on short notice. While new assets can start quickly, they require staying warm during downtime for rapid startup, often using auxiliary steam to maintain high temperatures and pressures. Here's an example where we're delivering an 8.2 megawatt precision electrode boiler that can quickly deliver high-pressure, high-temperature steam to enable rapid startup for a nuclear power plant. Other opportunities we see in this space are for refurbishment of existing facilities and small modular reactors known as SMRs. With that, I'd like to turn it over to our new CFO, Jan Schott, who will provide a more detailed review of our second quarter results before I wrap up with some remarks on our financial outlook. Jan?

Jan Schott | Chief Financial Officer:

Thank you, Bruce, and good morning, everyone. I'm very excited to be here with you all today. It has been less than a month since I joined Thermon, but it is already clear we have a strong finance team in place. I look forward to working with Bruce, the executive leadership team, and our finance organization as we continue to execute on our strategic plan and continue the tradition of strong execution and operational excellence at Thermon. I also look forward to meeting our analysts and investors and building strong relationships with the investment community. So with that, I will get into our financial review. During my discussion, I will provide some additional details on the quarter, give an update on our working capital and free cash flow, and conclude with a commentary on our balance sheet and liquidity. Moving now to slide nine and our second quarter performance. Revenue in the second quarter was \$115 million, a year-over-year decrease of 7.4%, as continued headwinds in our large project business was partially offset by the contribution from VaporPower and stable performance in our OpEx revenue. VaporPower contributed \$12.1 million of revenue during the second quarter. Excluding VaporPower, second quarter organic sales decreased 17%, versus a record 2024 quarter two. Large project revenue was 17.5 million during the second quarter, down 51% from the same period last year, as customers continue to delay decisions on large capital projects, as Bruce mentioned previously. This weakness was generally broad-based across our different market protocols. While large project spending was weak, Our OPEX revenues were \$97.2 million during the second quarter, an increase of 10% compared to last year, as our customers continue to prioritize maintenance and repair spending given the market uncertainty. Excluding vapor power, our OPEX revenues decreased 3.5% in the quarter. While we are disappointed in this result, the modest year-over-year decline, despite the challenging capital spending environment, demonstrates the benefits of our long-term customer relationships, deep installed base, and resilient OPEX spending. From a geographic perspective, we saw sales decline in U.S. Iamb, EMBA, and APAC, with a sales increase in Canada of 2%. We have seen the most pronounced decline in capital spending in U.S. Iamb. Adjusted EBITDA was \$23.8 million during the second quarter, down from \$27.7 million last year due to declines in our project revenue and continued investments in growth initiatives, partially offset by the contribution from vapor power and the benefits of our cost rationalization efforts. Adjusted EBITDA margins was 20.8% during the second quarter, down from 22.4% in the same period last year, largely due to volume shortfalls year over year. Margins benefited from an increased mix of materials revenue during the quarter, which generally carries higher growth margins. However, this is offset by the investments we continue to make in our strategic initiatives and lower project margins versus last year. During the second quarter, we completed the previously discussed consolidation of our rail and transit production lines from Denver into our San Marcos facility. which is part of our manufacturing rooftop consolidation program. As a result, we are on track to achieve our targeted \$5.7 million in annualized savings. We continue to expect just over \$4 million in realized savings during fiscal 25. Orders during the second

quarter were \$131.1 million compared to \$116.3 million in the same period last year, an increase of 13%. On an organic basis, orders increased 3%. We saw broad momentum in our order trends, highlighted by notable strength in Petrochem, transit, and oil and gas. Importantly, our decarbonization bookings increased 6% year over year, and over 70% of our incoming orders in the quarter were once again from diverse end markets. As a result of the solid order momentum, Backlog was 214.9 million at the end of the second quarter, up 29% compared to a backlog of 166.9 million as of the second quarter last year. Excluding backlog attributable to vapor power of 43.6 million, backlog increased 3% on an ordinary basis. Moving to slide 10, for an update on our balance sheet and liquidity, net working capital with 31.7% of sales during the quarter, down from 33.6% last year as we continue to optimize our supply chain while also improving lead times and on-time deliveries to our customers. CapEx was \$1.8 million during the second quarter of 25, down from \$2.8 million last year. As a result of our strict financial discipline, Free cash flow was \$6.7 million in the quarter, an improvement of \$6.1 million versus last year. Through the first half of the fiscal year, we have generated just over \$15 million in free cash flow versus the cash usage of \$1 million in the first half of last year. We expect our continued focus on working capital management, combined with our expectation of solid operating results, to deliver another year of strong free cash flow conversion. We paid down roughly \$3 million of term debt during the quarter, bringing our net debt balance to \$129 million. Net leverage was 1.3 times at the end of the second quarter. Net leverage is down from 1.5 times immediately following the acquisition of Safer Power. Based on our total cash and available liquidity, of \$129.8 million, we remain well capitalized and have ample flexibility to continue to support our capital needs. Assuming no additional acquisitions, we expect to target incremental debt pay down of \$20 to \$30 million during fiscal 25, combined with opportunistic share repurchases. In summary, we are pleased with our financial execution during the quarter as we made further progress on operational excellence initiatives and we generated strong free cash flow based on our stable operating performance and continued strict financial discipline. With that, I will turn the call back over to Bruce.

Bruce Sainz | Chief Executive Officer:

Thanks, Jan. Now if you'll turn to slide 11, we'll wrap up with our outlook for fiscal 2025. We continue to execute at a high level and are making important progress on our key strategic initiatives. I'm encouraged by our improved order trends over the last two quarters and am optimistic we'll see further momentum as we move forward. The long-term secular trends that positively impact many of our important end markets remain favorable, and we're well positioned to benefit from these drivers going forward. However, we're not totally immune to the weakness we're experiencing in the large project market and the push out of project timing. While over the last two quarters we're seeing the improved order momentum that was needed to drive our second half results, execution timelines of projects in backlog extend beyond our current fiscal year. As a result of these factors, we're adjusting our full year 2025 guidance as follows. We expect revenue in the range of \$495 million to \$515 million, which includes expected revenue from recent acquisitions. Adjusted EBITDA is now expected to range from \$105 to \$110 million, and adjusted EPS in a range of \$1.77 to \$1.89 per share. We think it's important to highlight that we continue to focus on our operational excellence initiatives and are carefully managing costs to current revenue levels, enabling us to protect earnings. Finally, just to wrap up things on slide 12, we're optimistic as ever for our business and the opportunities ahead remain as strong as ever. Our recent results demonstrate the progress we've made in developing a business that is more stable, profitable, and durable across cycles. Our large and growing installed base of loyal customers provides us with a resilient aftermarket franchise, which gives us access to a steady stream of predictable and highly profitable MRO revenues. We also remain well positioned to benefit from several powerful secular growth drivers, and these trends have not changed despite recent macroeconomic uncertainty. These secular drivers include the energy transition and decarbonization, on-shoring in North America, and infrastructure spending. We remain confident that these trends are as powerful as ever, and we believe that the recent spending delays only serve to create pent-up demand when customer confidence improves. Lastly, we benefit from a high margin, low capital intensity business that yields significant cash flow. As Jan covered earlier, our free cash flow through the first half is up meaningfully from last year, and we continue to maintain a strong financial position. This provides us the flexibility to pursue our capital allocation

priorities, and we've demonstrated this commitment to our strategy through the recent acquisitions of Vapor Power and FOTI, ongoing investments in organic growth initiatives, and execution under our share repurchase plan, all with a focus on creating long-term shareholder value. That completes our prepared remarks. We're now ready for the question and answer portion of our call.

Operator | Conference Operator:

Thank you. Ladies and gentlemen, the floor is now open for questions. If you would like to ask a question, please press star 1 on your telephone keypad at this time. A confirmation tone will indicate your line is in the question queue. You may press star 2 if you would like to withdraw your question from the queue. For participants using speaker equipment, it may be necessary to pick up the handset before pressing the star keys. Again, that's star 1 to register a question. Today's first question is coming from Justin Ages of CGS Securities. Please go ahead.

Justin Ages | Analyst, CGS Securities:

Hi, good morning, and thanks for taking the questions. Hey, good morning, Justin. And I look forward to working with you, Jan.

Jan Schott | Chief Financial Officer:

Yes, absolutely. Nice to meet you on the phone.

Justin Ages | Analyst, CGS Securities:

Yeah. And first question I have, the sales guidance, in the past you've given the contribution from VaporPower. Can you give us any indication whether that's still tracking towards \$55 million just kind of want to triangulate an organic growth for the sales guidance?

Bruce Sainz | Chief Executive Officer:

Yes. So, yes, we do believe that the vapor business is still tracking in that \$55 to \$57 million range, looking forward for the balance of the year. Our backlog there is quite strong, so the real challenge is growing capacity to – to ship, and should we be able to execute on that? We could possibly see some upside, but right now we're forecasting in that \$55 to \$57 million range, and that's included in the guidance. Okay.

Justin Ages | Analyst, CGS Securities:

That's helpful. Thanks. And the next, last question, if I could, you know, interesting to call out the presence in nuclear given the you know, data center demand. Can you give us any more color on this current size of what that end market is to your business or any other details?

Bruce Sainz | Chief Executive Officer:

Yeah, so as we look at just the pipeline of opportunities, in the pipelines roughly about 1.2 billion, we see the current nuclear opportunities roughly about 4% of that. We have some other very large opportunities that are not included in that number. One is a large expansion of an existing facility, and another is around small modular reactors. Those are about 100 million, but they've not necessarily – there's not plans yet to move

forward. So we're seeing some growing opportunities in that space.

Justin Ages | Analyst, CGS Securities:

All right, thanks. I appreciate you taking the question.

Bruce Sainz | Chief Executive Officer:

Thank you, Justin.

Operator | Conference Operator:

Thank you. The next question is coming from Brian Drapp of William Blair. Please go ahead.

Brian Drapp | Analyst, William Blair:

Good morning. Thanks for taking my questions, Jan. Nice to meet you. Looking forward to working with you. Nice to meet you. Yep. I first just wanted to ask about the large project activity. I guess I'm wondering, now that we're past the election, does that affect the probability that some of these projects start to get released and or is that really not what was holding it up, and just what's the outlook for some of that activity coming back?

Bruce Sainz | Chief Executive Officer:

Yeah, Ryan, you know, I can't necessarily speak for customers, but, you know, they're certainly with the elections behind us. I think you get clarity moving forward, and certainly policy is going to drive pace, so I think that will be important, and I think there'll be more clarity moving forward. So, you know, we believe it's probably going to have a positive impact on overall activity. The good news is we continue to see that pipeline of opportunities grow and we actually began to see some of these projects move forward during the quarter. I noted a couple of them, one in a large carbon capture petrochemical project and the other a large multi-year rail and transit project that's tied to infrastructure spending. Those are a couple of examples of what we're seeing. And certainly as we look at the pipeline of opportunity in quotations, it would indicate that the opportunities ahead are growing, not contracting. So at some point we would expect customers to begin to move forward.

Brian Drapp | Analyst, William Blair:

Okay. And then the next question just on the weather and thinking back to last year and the unusually warm weather. whether we had in Canada in particular, what are you seeing as you're heading into the, you know, getting into the heating season now? And, you know, are you, you know, you have some very easy comps, obviously, with the weather. And I guess I'll just leave it there for a second, and then I have a follow-up on that.

Bruce Sainz | Chief Executive Officer:

Yeah, so I'm not a meteorologist, so I can't predict the weather, but we are seeing nice material sales, which we noted during the quarter, and that has continued into the beginning of this quarter, so we see that momentum. We also are just expectations as we're planning. We're planning for more of a normalized winter ahead. I mean, that's typically how we plan, and As we look at this, when we look at just the weakness in revenues, it's really on the large capital project side. And as I said, our backlog, our organic backlog is growing. So we had two positive book-to-bill quarters. This quarter, we actually saw year-over-year bookings growth. So we see that backlog growing. Right now, just the bulk of those projects, the time of execution is out into early 26. And right now, we're heavily involved in engineering and design in anticipation of material shipments and any field execution.

Brian Drapp | Analyst, William Blair:

Okay. And then I was just going to say, can you remind me, isn't some of that product that you ship into the Canadian region, I guess, I think it's some of the mineral insulated cable, if I remember correctly, is relatively high margin. And I'm just wondering, I'm trying to, you know, if there's a positive year over year comparison coming potentially if this, you know, there's a lot of talk about like a La Nina winter and who knows if, if, uh, again, we're not meteorologists obviously, but, um, trying to find, you know, opportunity here.

Bruce Sainz | Chief Executive Officer:

Well, I would, uh, I would make a couple of comments. First of all, if you recall last year, our Canadian business was quite weak. Uh, coming into this year, our Canadian business has actually is actually up year over year. So, We've seen that not only bottom out, but begin to improve. So I would just say that is more on the general business activity and overall economic conditions we're seeing. So I think that's certainly a positive sign. And then as you say, our Canadian operations, because of the harsh climates, they tend to have the very high temperature types of products, which tend to drive a higher margin profile. So, yes, stronger sales in Canada equals better gross margins, certainly.

Brian Drapp | Analyst, William Blair:

And then just the last question, can you repeat what you said about the decarbonization pipeline? I just missed the number that you said. What percentage of the 1.2 is that, and how did that grow?

Bruce Sainz | Chief Executive Officer:

It's grown to roughly 320 million of that 1.2 billion. Got it.

Brian Drapp | Analyst, William Blair:

Thank you very much.

Bruce Sainz | Chief Executive Officer:

Thank you.

Operator | Conference Operator:

Once again, ladies and gentlemen, that is Star 1. If you would like to ask a question. Our next question is coming from John Bratz of Oppenheimer. Please go ahead.

John Bratz | Analyst, Oppenheimer & Co.:

Good morning, everyone. And Jan, welcome aboard.

Jan Schott | Chief Financial Officer:

Thanks so much. Look forward to working with you.

John Bratz | Analyst, Oppenheimer & Co.:

Bruce, I don't know. Maybe I missed it, but the large projects that are being pushed out, are they in the your more traditional oil and gas markets, or are they elsewhere?

Bruce Sainz | Chief Executive Officer:

Right now, overall, our oil and gas activity, I would say, is down as we look at this and we look at the project opportunities and large capital projects. First and foremost, just our backlog of those opportunities are down, but then also we see some execution, and I would I would say we're seeing timing of some of these change. It's broad-based. There's some large projects in renewables that we're seeing being somewhat delayed due to some permitting issues. We've got things that are just typical project delays. Execution is lagging. Particularly, there's one large project in semiconductors that's lagging. We've got a large pharmaceutical project that we would expect to start to generate revenues later this year. It's in the engineering stages. So there's just, if you think about the project timing, a lot of the projects we have now are in engineering. And the large petrochemical project we just booked with carbon capture storage, that's going to be in engineering for the back half of this year, and revenues will start early in 26. So What we see is some nice momentum building into 26 as we grow the backlog, and we see order activity improve on larger capital projects.

John Bratz | Analyst, Oppenheimer & Co.:

Okay, okay. Bruce, in your conversations with your customers, clients, obviously we have a new administration coming in who sort of favors oil and gas, drill to baby drill, and do you get the sense that any of these alternative energy projects, decarbonization, things like those might be put more on a back burner and there's more of an emphasis on oil and gas. Do you think there's going to be any shift in the business opportunities that you're seeing currently?

Bruce Sainz | Chief Executive Officer:

You know, I think first and foremost, The reduction in uncertainty by having a known outcome I think is positive overall for business. I think the good news is that we stand to benefit no matter which direction policy takes us going forward. We have still 30% of our revenues are in the oil and gas sector and will benefit if those spending patterns improve and Conversely, we've got opportunities in the decarbonization space as well. It'll be interesting to see how policy evolves and impacts. I think if you look historically, there are certain areas that spending may be favored, particularly as you look at how the IRA dollars may be spent that will support certain technologies and maybe challenge others. So, you know, I think policy will drive pace and

we'll see that evolve over the next, say, six to 12 months.

John Bratz | Analyst, Oppenheimer & Co.:

Okay. Okay. And, Jan, the SG&A spend maybe a little bit more than what I was looking for. You talk about spending on some of the initiatives to develop your business further. Would you see that spending rate continuing on for a while or is some of the heavier spending behind us now?

Jan Schott | Chief Financial Officer:

I think going forward we would expect that to trend downward. We did see an increase in SG&A for the vapor power acquisition this quarter, but our organic was actually 3% down. Okay. And that's consistent with our long-term strategy.

John Bratz | Analyst, Oppenheimer & Co.:

Okay. Thank you, Jen.

Operator | Conference Operator:

Thank you. Once again, that is star one for any final questions. At this time, I'd like to turn the floor back over to Mr. Thames for closing comments.

Bruce Sainz | Chief Executive Officer:

All right. Thank you, Donna. And again, I'd like to thank all of our Thermon employees around the globe that are serving our customers with excellence each and every day. So thank you for all that you do. And I'd also like to thank all of you for your time and your interest in Thermon. And if we don't speak during the quarter, I look forward to spending time with you on our next quarterly call. So thank you and have a good day.

Operator | Conference Operator:

Ladies and gentlemen, thank you for your participation. This concludes today's event. You may disconnect your line to log off the webcast at this time and enjoy the rest of your day.