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Fiscal Q4 2019 Recap

August 14, 2019

Safe Harbor Statement

All forward-looking statements are based on current expectations regarding important risk factors, including trends in the industrial sector of the economy, the success of our various marketing strategies, and other risk factors identified in Applied's most recent periodic report and other filings made with the SEC. Accordingly, actual results may differ materially from those expressed in the forward-looking statements.

Non-GAAP Financial Measures

This presentation sets forth certain non-GAAP financial measures - Adjusted Earnings per Share (EPS), Adjusted Net Income, EBITDA, Free Cash Flow, Net Leverage Ratio - which are presented as supplemental disclosures to Net Income, Cash from Operations, Total Debt Outstanding, and reported results. Management believes these measures are useful indicators for normalizing earnings for non-routine items and facilitating effective evaluation of operating performance. A presentation of the most directly comparable GAAP measure and reconciliations of Adjusted EPS, Adjusted Net Income, EBITDA, Free Cash Flow, and Net Leverage Ratio are set forth in the appendix to this presentation.

Primary Messages from Management

- Fiscal Q4 FY19 EPS toward high end of guidance excluding discrete tax items.
- Gross margin expansion excluding LIFO expense and SD&A control offset weaker sales, highlighting adaptable cost structure, execution, and self-help opportunities.
- Cash generation exceeds revised guidance; remain confident in FY20 cash outlook given inventory and other working capital actions.
- Consolidated sales declined YoY reflecting broad end-market slowing, ongoing Fluid Power technology market headwinds, and difficult prior year comparisons.
- Sales in U.S. Service Center operations increased YoY, while Fluid Power technology market headwinds remain stable with backlog improving sequentially.
- Initial FY20 sales and EPS guidance assumes cautious end-market outlook.
- Announce entrance into machine/robotic automation with definitive agreement to acquire Olympus Controls.

Fiscal Q4 2019 Key Financial Highlights

- **Sales down 1.7% YoY**
  - Down 2.7% days adjusted organic
    - *Up 6% on a two-year stack basis*
  - Acquisitions +2.2%, currency -0.4%, days -0.8%
- **Gross margin up 15 bps YoY excluding LIFO expense ($3.3M or 37 bps)**
- **SD&A expense down 3.9% YoY**
  - 21.0% of sales = 50 bps improvement YoY
- **Net Income of $40M; EPS of $1.02**
  - Includes $0.18 of discrete tax expense primarily from U.S. tax reform and the offset of a tax benefit recognized in Q1 FY19 related to the one-time transition tax
  - EPS near high end of guidance ($1.11-$1.21) excluding discrete tax expense in quarter
- **EBITDA $88M, up 0.6% YoY including -3.8% from incremental LIFO expense**
  - 9.9% of sales, up 23 bps YoY (60 bps ex LIFO)

Key Quarter Discussion Points

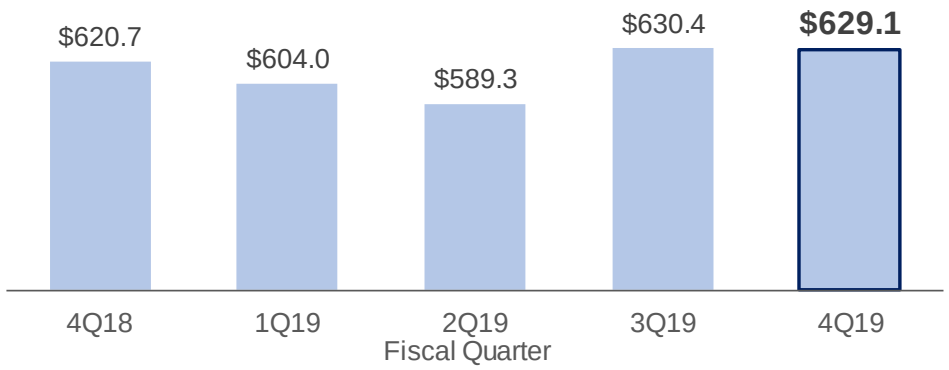
Discussion Point	Update	Detail
1. Industrial Demand	• *Volumes slowed broadly in April/May across a variety of end markets with some stabilization in June*	• *Service Center segment organic daily sales up 0.5% YoY and down 3% sequentially in Q4*
2. Inflation; Price/Cost	• *Headwinds remain but offsetting through positive pricing traction and self-help margin initiatives*	• *Q4 gross margins up 15 bps YoY excluding LIFO headwind with price/cost trends largely neutral*
3. Cash Generation	• *Solid Q4 rebound from weaker Q3 trends; remain positive on FY20 cash generation potential*	• *Q4 Cash from Operations $103M; Free Cash $96M (242% of net income)*
4. Fluid Power Sales	• *Tech market remains drag but headwind stabilizing; demand in other OE end markets slower*	• *Fluid Power sales flat YoY in Q4 excluding tech end-market sales*
5. SD&A Control	• *Execution and self-help initiatives supporting margins; additional opportunities in slower environment*	• *Down more than 5% YoY organically in Q4*
6. FCX Update	• *Slower demand in process end markets and non-recurring prior year project activity impacting YoY sales*	• *Reaffirm FCX $30M synergy target*
7. M&A Update	• *Remains high priority with pipeline active and full*	• *Entrance into machine/robotics automation with definitive agreement to acquire Olympus Controls*

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Segment Results – Service Center Based Distribution

Segment Overview: *Representing 71% of fiscal 2019 sales - the segment includes our legacy distribution operations including more than 430 local service centers across North America, Australia, and New Zealand, primarily focused on our core bearings, power transmission, and fluid power MRO product offering, as well as other industrial supplies for scheduled maintenance and emergency repairs of customers' machinery and equipment. The segment also includes our upstream oil & gas focused operations centered primarily within the Permian Basin.*

Service Center Distribution Sales, in Millions



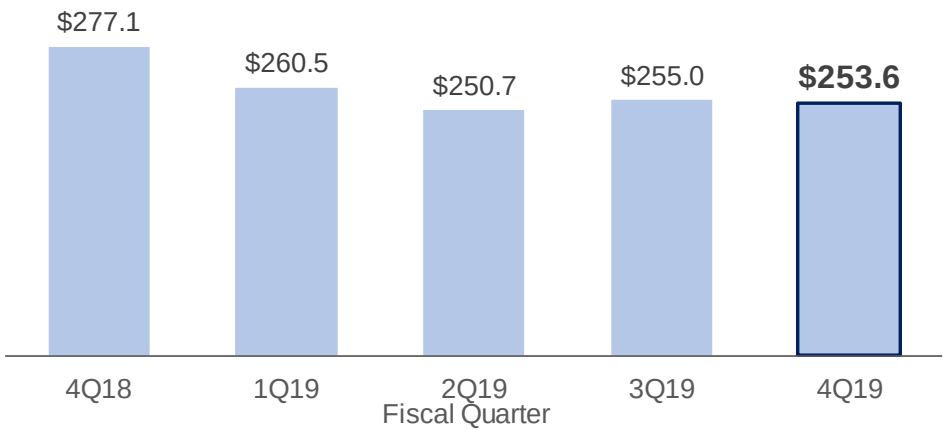
- **Sales up 1.4% YoY**
  - Days Adj. Organic +0.5% (*Up 9% on a two-year stack basis)*
  - Selling Days - 0.8%
  - Currency - 0.5%
  - Acquisitions +2.2%
- **Sales per day down 3% from Q3**
- **Segment sales supported by ongoing positive growth in U.S. Service Center operations despite slower end markets and difficult prior year comparisons**

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Segment Results – Fluid Power & Flow Control

Segment Overview: *Representing 29% of fiscal 2019 sales - the segment consists of our legacy Fluid Power network specializing in distributing, engineering, designing, integrating, and repairing hydraulic and pneumatic technologies, as well as our engineered flow control products and services business following our acquisition of FCX Performance in fiscal 2018.*

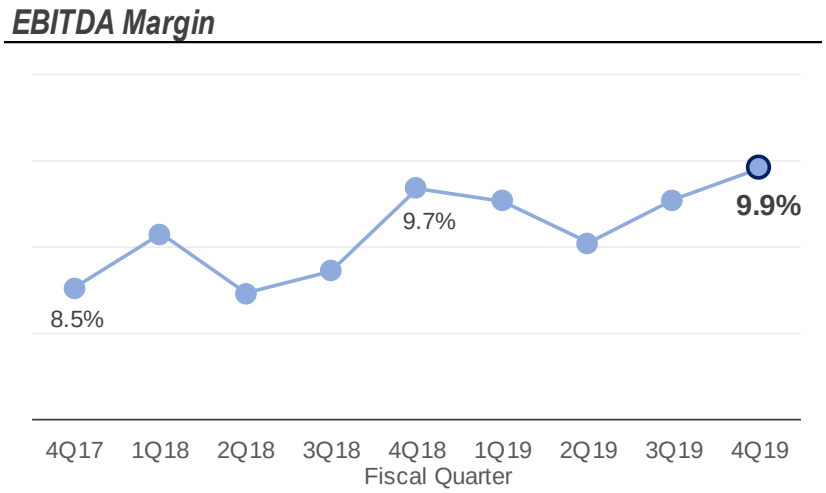
Fluid Power & Flow Control Sales, in Millions



- **Sales down 8.5% YoY**
  - Days Adj. Organic - 9.8%
  - Selling Days - 0.8%
  - Acquisitions +2.1%
- **Sales per day down 1% from Q3**
- **YoY sales decline reflects ongoing Fluid Power technology market headwinds, as well as slower Flow Control sales**
- **Fluid Power sales flat YoY organically excluding technology end market**
  - Related backlog up sequentially past four months

Margin and Expense Highlights

$ in millions	Q4 FY19	Q4 FY18	% Chg YoY	Excluding LIFO % Chg YoY
Gross Profit	**$257.4**	$263.7	(2.4%)	(1.2%)
Gross Margin	**29.2%**	29.4%	(22) bps	15 bps
SD&A Expense	**$185.4**	$192.9	(3.9%)	
% of Sales	**21.0%**	21.5%	50 bps	
EBITDA	**$87.6**	$87.0	0.6%	4.4%
EBITDA Margin	**9.9%**	9.7%	23 bps	60 bps
Memo:				
LIFO Expense	**$3.4**	$0.2		

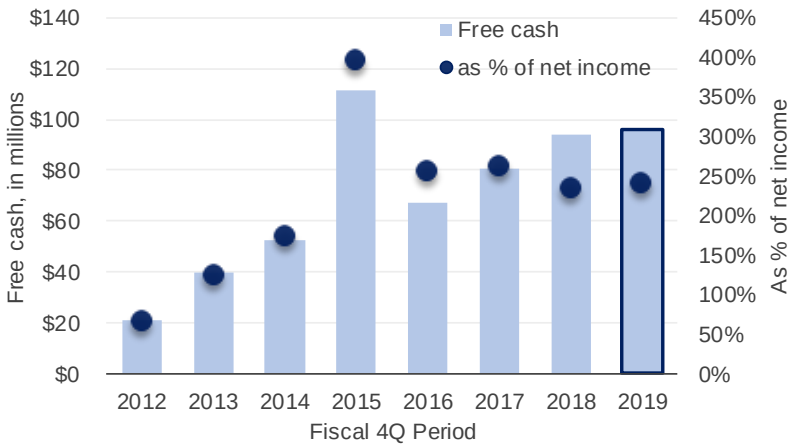


- **Gross margin down 22 bps YoY, up 20 bps sequentially**
  - Excluding LIFO expense, up 15 bps YoY
  - Ongoing price traction and internal initiatives helping offset broader inflation
- **SD&A expense down 3.9% YoY**
  - Organic - 5.1%
  - Currency - 0.5%
  - Acquisitions +1.7%
- **EBITDA margin up 23 bps YoY including incremental LIFO expense**

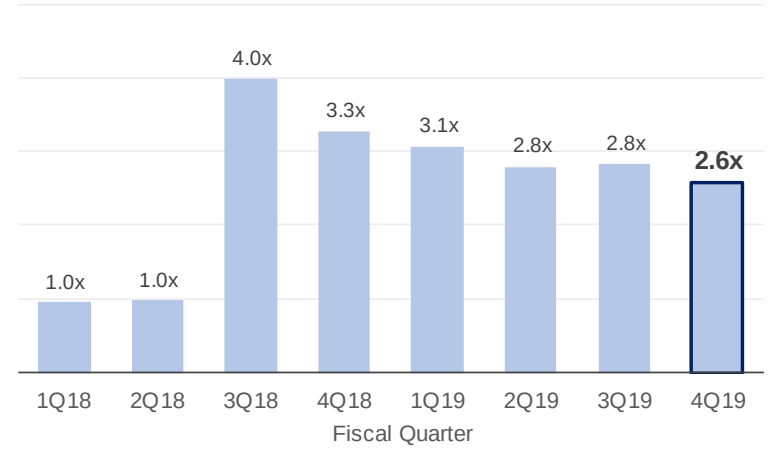
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Cash Flow and Balance Sheet

Fiscal 4Q Free Cash Flow, in Millions



Net Leverage Ratio (Net Debt to Trailing EBITDA)



- **Q4 2019 cash from operations of $103M; free cash of $96M**
  - Free cash up 2% YoY; 240% of net income; exceeded guidance of $40M to $85M
  - Ongoing traction with working capital initiatives
- **Full-year FY19 cash from operations of $181M; free cash of $162M**
  - Free cash up 30% YoY; 94% of adjusted net income
  - Returned over $58M to shareholders via dividends and share buybacks
- **Net leverage ratio at ~2.6x**
  - Below prior year of 3.3x
  - Paid down $24M of outstanding debt in Q4, nearly $104M since financing FCX acquisition

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Full-Year Fiscal 2019 Summary

	Fiscal 2019	Key Underlying Trend During the Year
Sales	**$3.473B**	*Record level - Up 13% including 2% organically*
Gross Margin	**29.0%**	*Up 25 bps or 53 bps excluding incremental LIFO expense*
SD&A Expense (1)	**$740.6M**	*Flat organically excluding prior year deal costs*
Adjusted Net Income (1)	**$172.6M**	*Record level - Up 18% excluding prior year deal costs*
EBITDA	**$328.4M**	*Record level - Up 18%, or 6% organically excluding prior year deal costs*
EBITDA Margin	**9.5%**	*Up 41 bps or 73 bps excluding incremental LIFO expense*
Adjusted EPS (1)	**$4.41**	*Up 18% excluding prior year deal costs*
Free Cash	**$162M**	*Up 30% and over 90% of adjusted net income*

(1) Excludes non-recurring impairment and restructuring expense during 3Q 2019

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Fiscal 2020 Outlook and Guidance

- **Sales down 2% to up 2%**
  - Days adjusted organic ➡ - 5% to -1%
  - Acquisitions ➡ + 2%
  - Selling Days ➡ + 1%
- **EPS of $4.20 to $4.50**
- **Free cash of $200M to $220M**
- **Other assumptions:**
  - Interest expense ➡ $37M to $38M
  - Tax rate ➡ 25% to 26%
  - Diluted share count ➡ 39M

Key Investment Considerations Entering Fiscal 2020

- **Strong and consistent free cash generation with upside potential**
  - *Improving margin profile and working capital (intermediate target 20% of sales vs. 22%-23% currently)*
- **Consistent margin improvement supported by self-help initiatives**
  - *Target gross margin expansion, high-teen incremental margins over a cycle*
- **History of cost discipline and margin/earnings support in slowdown**
  - *See ongoing self-help opportunities and reinforcing expense focus given demand uncertainty*
- **Share gain opportunity and competitive moat from technical focus**
  - *Technical / engineering capabilities and service solutions increasingly critical across customer base*
- **Disciplined capital deployment on M&A**
  - *Remain focused on accretive M&A with proprietary pipeline active and full, supporting growth profile*
- **Market position creates opportunities around IIoT and automation**
  - *Agreement to acquire Olympus Controls; engaging customers & suppliers on smart products & solutions*
- **Enhanced earnings power versus prior cycles**
  - *More diversified growth profile; sales up 26% and EBITDA margins up 130 bps vs. prior peak levels*

Appendix: Reconciliation of Adjusted Net Income and EPS

	Net Income Impact Year Ended June 30,		Per Share - Diluted Impact Year Ended June 30,	
	2019	2018	2019	2018
Net Income and Net Income Per Share	**$ 143,993**	**$ 141,625**	**$ 3.68**	**$ 3.61**
Adjustments:				
FCX one-time costs	-	5,128	-	0.13
Canadian intangible impairment	23,109	-	0.59	-
Canadian tax valuation allowance	3,785	-	0.10	-
Restructuring costs	1,702	-	0.04	-
Adjusted Net Income and Adjusted EPS	**$ 172,589**	**$ 146,753**	**$ 4.41**	**$ 3.74**

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Appendix: Reconciliation of EBITDA

(In thousands)	Three Months Ended June 30, 2019	Three Months Ended June 30, 2018	Year Ended June 30, 2019	Year Ended June 30, 2018
Net Income	**$ 39,803**	**$ 40,362**	**$ 143,993**	**$ 141,625**
Interest expense, net	10,187	10,964	40,188	23,485
Income tax expense	22,317	19,859	50,488	63,093
Depreciation and amortization of property	5,191	5,077	20,236	17,798
Amortization of intangibles (including impairment)	10,060	10,739	73,477	32,065
EBITDA	**$ 87,558**	**$ 87,001**	**$ 328,382**	**$ 278,066**

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Appendix: Reconciliation of Free Cash Flow

(in thousands)	Three Months Ended June 30							
	Q4 FY12	**Q4 FY13**	**Q4 FY14**	**Q4 FY15**	**Q4 FY16**	**Q4 FY17**	**Q4 FY18**	**Q4 FY19**
Cash provided by Operating Activities	**$ 28,451**	**$ 42,341**	**$ 65,784**	**$115,226**	**$ 69,696**	**$ 86,113**	**$ 99,426**	**$103,435**
Capital expenditures	(7,726)	(2,378)	(13,698)	(3,924)	(3,689)	(5,258)	(5,332)	(7,259)
Free Cash Flow	**$ 20,725**	**$ 39,963**	**$ 52,086**	**$111,302**	**$ 66,007**	**$ 80,855**	**$ 94,094**	**$ 96,176**

(in thousands)	Year Ended June 30	
	2019	**2018**
Cash provided by Operating Activities	**$180,602**	**$147,305**
Capital expenditures	(18,970)	(23,230)
Free Cash Flow	**$161,632**	**$124,075**

Appendix: Reconciliation of Net Leverage Ratio

	Three Months Ended June 30										
	Q2 FY17	Q3 FY17	Q4 FY17	Q1 FY18	Q2 FY18	Q3 FY18 [1]	Q4 FY18	Q1 FY19	Q2 FY19	Q3 FY19	Q4 FY19
Net Income	$ 24,085	$ 29,494	$ 52,960	$ 33,721	$ 30,950	$ 36,592	$ 40,362	$ 48,938	$ 38,717	$ 16,535	$ 39,803
Interest expense, net	2,100	2,165	2,130	2,166	2,139	8,216	10,964	10,476	9,578	9,947	10,187
Income tax expense	11,682	13,855	(6,580)	16,661	13,646	12,927	19,859	7,164	11,724	9,283	22,317
Depreciation and amortization of property	3,837	3,877	3,942	3,927	4,081	4,713	5,077	4,981	5,038	5,026	5,191
Amortization of intangibles (including impairment)	6,094	6,056	5,984	5,831	5,695	9,800	10,739	10,921	10,991	41,505	10,060
EBITDA	$ 47,798	$ 55,447	$ 58,436	$ 62,306	$ 56,511	$ 72,248	$ 87,001	$ 82,480	$ 76,048	$ 82,296	$ 87,558
Trailing 4-Quarter EBITDA				223,987	232,700	249,501	278,066	298,240	317,777	327,825	328,382
Current portion of long-term debt				$ 5,595	$ 6,378	$ 19,182	$ 19,183	$ 19,184	$ 44,184	$ 44,163	$ 49,036
Long-term debt				285,175	306,579	1,017,327	944,522	953,216	923,410	937,536	908,850
Total Debt				$ 290,770	$ 312,957	$1,036,509	$ 963,705	$ 972,400	$ 967,594	$ 981,699	$ 957,886
Cash				77,769	85,324	43,523	54,150	56,408	79,827	47,367	108,219
Net Debt				$ 213,001	$ 227,633	$ 992,986	$ 909,555	$ 915,992	$ 887,767	$ 934,332	$ 849,667
Net Leverage Ratio				**1.0**	**1.0**	**4.0**	**3.3**	**3.1**	**2.8**	**2.9**	**2.6**

(1) The increase in the Net Leverage Ratio during Q3 FY18 reflects the financing of our FCX acquisition

Appendix: Number of Selling Days by Fiscal Quarter and Full Year

	Q1	Q2	Q3	Q4	Year
2018	63.0	61.0	63.5	64.0	251.5
2019	63.0	62.0	63.0	63.5	251.5
2020	**64.0**	**62.0**	**64.0**	**63.5**	**253.5**