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Q1 2021 Garmin Ltd Earnings Call

EVENT DATE/TIME: APRIL 28, 2021 / 2:30PM GMT

CORPORATE PARTICIPANTS

Clifton Albert Pemble *Garmin Ltd. - President, CEO & Director*
Douglas Gerard Boessen *Garmin Ltd. - CFO & Treasurer*
Teri Seck *Garmin Ltd. - Manager of IR*

CONFERENCE CALL PARTICIPANTS

Benjamin James Bollin *Cleveland Research Company - Senior Research Analyst*
Derek John Soderberg *Colliers Securities LLC, Research Division - Senior Research Analyst*
Erik William Richard Woodring *Morgan Stanley, Research Division - Research Associate*
Ivan Philip Feinseth *Tigress Financial Partners LLC, Research Division - Director of Research*
Jeffrey A. Rand *Deutsche Bank AG, Research Division - Research Associate*
Nikolay Todorov *Longbow Research LLC - Analyst*
Paul Chung *JPMorgan Chase & Co, Research Division - VP & IT Hardware Analyst*
William Verity Power *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

PRESENTATION

Operator
Thank you for standing by, and welcome to the Garmin Ltd. First Quarter 2021 Earnings Call. (Operator Instructions) Please be advised that today's call is being recorded. (Operator Instructions) I would now like to hand the call over to Teri Seck, Investor Relations. Please go ahead.

Teri Seck ***Garmin Ltd. - Manager of IR***
Good morning, everyone. We would like to welcome you to Garmin Ltd's First Quarter 2021 Earnings Call. Please note that the earnings press release and related slides are available at Garmin's Investor Relations site on the internet at www.garmin.com/stock. An archive of the webcast and related transcript will also be available on our website.

This earning call includes projections and other forward-looking statements regarding Garmin Ltd. and its business. Any statements regarding our future financial condition, revenues, earnings, gross margins, operating margins, future dividends, market shares, product introduction, future demand for our products and plans and objectives are forward-looking statements. The forward-looking events and circumstances discussed on this earnings call may have occurred. Actual results could differ materially as a result of various factors affecting Garmin. Information concerning these risk factors is contained in our Form 10-K filed with the Securities and Exchange Commission. In particular, there's significant uncertainty about the duration and impact of the COVID-19 pandemic. This means that results could change at anytime, and any statement about the impact of COVID-19 on the company's business results and outlook is the best estimate based on the information available as of today's date.

Presenting on behalf of Garmin Ltd. this morning are Cliff Pemble, President and Chief Executive Officer; and Doug Boessen, Chief Financial Officer and Treasurer. At this time, I'd like to turn the call over to Cliff

Pemble.

Clifton Albert Pemble ***Garmin Ltd. - President, CEO & Director***

Thank you, Teri, and good morning, everyone. As announced earlier today, 2021 began on a strong note as momentum from 2020 continued into the new year. Consolidated revenue came in at nearly $1.1 billion, up 25% over the prior year with strong double-digit growth in 4 of our 5 business segments. Gross margin was strong at 59.8%. Operating margin increased to 23.3% and operating income grew 41% to $250 million. This resulted in GAAP EPS of $1.14. Pro forma EPS was $1.18, up 30% over the prior year.

Before turning the call over to Doug, I'll provide highlights by segment and a summary of what we see ahead.

Starting with fitness, revenue increased 38% to $308 million, driven by strong demand for cycling products and advanced wearables. Gross and operating margins were 56% and 24%, respectively. Operating income more than doubled over the prior year to $74 million. During the quarter, we introduced Lily, a fashion-first smart watch with exceptional features designed specifically for women. In the cycling market, we launched the Rally power meters, including a version for off-road cycling, which is a new product category for us.

Moving to outdoor. Revenue increased 46% to $256 million with growth across all product categories led by strong demand for adventure watches. The outdoor segment generated strong growth and operating margins of 67% and 36%, respectively. Operating income nearly doubled over the prior year to $93 million. During the quarter, we launched Enduro, a new adventure watch category built specifically for athletes who demand exceptional battery life for endurance racing. We also expanded the Approach family of golf tracking devices with the launch of 3 new products for golfers of every skill level.

Looking next at aviation. Revenue decreased 8% to $174 million, driven primarily by reduced contributions from ADS-B products that remained strong in the first quarter of 2020. Excluding the impact from ADS-B, revenue was relatively flat to last year, which is an encouraging signal that the underlying market has stabilized. Gross and operating margins were 73% and 26%, respectively.

During the quarter, Autoland was selected as 1 of 7 finalists for the Robert J. Collier Trophy. The Collier Trophy is a prestigious award that recognizes significant achievements in the areas of aeronautics and astronautics. In addition, we recently added several aircraft models to the list of GFC500 and 600 autopilot certifications, which expands the addressable market for these advanced flight control systems.

Looking next at the Marine Segment. Revenue increased 28% to $209 million. Gross and operating margins were 58% and 29%, respectively. Operating income increased 53% over the prior year to $62 million. During the quarter, we experienced strong demand for chartplotters and Panoptix LiveScope sonars from new boat manufacturers and users preparing their boats for the upcoming season on the water.

Looking finally at auto. Revenue increased 18% to $124 million, and we experienced growth in both OEM and consumer categories. Gross margin was 39% and, and we recorded an operating loss of $24 million, driven by ongoing investments in OEM programs for next-generation vehicles. During the quarter, we entered the powersports market with a full complement of products designed to help recreational off-roaders find their way, stay connected with other riders, control electrical systems on the vehicle and monitor their surroundings.

In summary, Q1 was another record-breaking quarter. We're very pleased with what we've accomplished so far this year, and we continue to see strong demand for our products. Some of you are wondering how this strong performance affects our outlook for the rest of the year. We believe there are 2 very important factors to consider. First, much of the year remains ahead of us. Q1 is typically the lowest seasonal quarter of our financial year. It's difficult to predict what the remainder of the year will look like based on 1 period, especially considering the pandemic-driven dynamics of the past year.

Second, the electronics industry is experiencing high demand for and short supply of certain electrical components. So far, the impact on us has been minimal due to our inventory strategy and vertically integrated business model. However, the situation is very dynamic, complex and long term in nature and, thus, difficult to predict how it will evolve. With these things in mind, we're maintaining the guidance issued on February 17, 2021. So that concludes my remarks. Next, Doug will walk you through additional details on our financial results. Doug?

Douglas Gerard Boessen ***Garmin Ltd. - CFO & Treasurer***

Thanks, Cliff. Good morning, everyone. I'm reviewing our first quarter financial results and make comments on the balance sheet, cash flow statement and taxes. We posted revenue of $1.072 billion in the first quarter, representing 25% increase year-over-year. Gross margin was 59.8%, a 60 basis point increase. Operating expense as a percentage of sales was 36.5%, a 200 basis point decrease. Operating income was $250 million, 41% increase. Operating margin was 23.3%, 260 basis point increase. Our GAAP EPS was $1.14. Pro forma EPS was $1.18.

Next we will look at our first quarter revenue by segment and geography. For the first quarter, we achieved double-digit growth in 4 of our 5 segments led by the outdoor segment with strong growth of 46% followed by the fitness segment with 38% growth and the marine segment with 28% growth. By geography, we achieved double-digit growth in all 3 regions led by strong growth of 33% in EMEA and 31% growth in APAC. Americas grew 18%, which is more heavily impacted by the decline in aviation. Excluding aviation, Americas' growth was more in line with the other regions.

Next, operating expenses. First quarter operating expenses increased by $62 million or 19%. Research and development increased $38 million year-over-year, primarily due to engineering personnel costs across all of our segments, and other expenses related to Auto OEM Programs. Our advertising expense increased approximately $4 million due to higher spend in the outdoor and fitness segments. SG&A increased $20 million compared to prior year quarter, but decreased as a percentage of sales to 14.7%, a

130 basis point decrease compared to the prior year. The increase in SG&A was primarily due to increase in personnel-related expenses, and information technology costs.

A few highlights on the balance sheet, cash flow statement and taxes. We ended the quarter with cash, and marketable securities of approximately $3.2 billion. Accounts receivable decreased sequentially to $558 million following a seasonally strong fourth quarter. Inventory balance increased year-over-year to $838 million. In the first quarter 2021, we generated free cash flow of $331 million, $147 million increase the prior quarter. During the first quarter 2021 we reported an effective tax rate of 12.2% compared to 9.3% in the prior year quarter. The increase in effective tax rate is primarily due to larger amount of reserve releases in the prior year. This concludes our formal remarks. Michelle, can you please open the line for Q&A?

Teri Seck ***Garmin Ltd. - Manager of IR***

Thanks, everyone, for your time today. Doug and I are available for callbacks and we hope you have a great day. Bye.

Operator

Ladies and gentlemen, this does conclude the conference. You may now disconnect. Everyone, have a great day.