STRATTEC

STRATTEC SECURITY CORPORATION

SECOND QUARTER FISCAL YEAR 2026
EARNINGS RESULTS CONFERENCE CALL TRANSCRIPT

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PRESENTERS

Jennifer Slater
President and Chief Executive Officer

Matthew Pauli
Senior Vice President, Chief Financial Officer

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John Franzreb
Sidoti & Company

Brian Sponheimer
Gabelli Funds LLC

Presentation

Operator

Greetings. Welcome to STRATTEC Security Corp. operations second quarter of Fiscal Year 2026 Financial Results call. At this time, all participants are in a listen only mode. A question-and-answer session will follow the formal presentation. If anyone should require operator assistance during the conference, please press Star Zero on your telephone keypad. Please note this conference is being recorded. I will now turn the call over to Deborah K. Pawlowski Investor Relations. Thank you. You may begin.

Deborah K. Pawlowski
Investor Relations

Thank you, and good morning, everyone. We appreciate you joining us for Strattec's second quarter fiscal 2026 financial results conference call. Joining me on the call this morning are Jennifer Slater, President and CEO, and Matthew Pauli, Vice President and Chief Financial Officer.

Jen and Matt will review our financial results, the progress being made to transform Strattec, and our outlook. You can find a copy of the press release and the slides that accompany our conversation today on the investor relations section of the Company's website.

If you are reviewing those slides, please turn to **Slide 2** for the safe harbor statement. As you are aware, we may make some forward-looking statements on this call during the formal discussion as well as during the Q&A. These statements apply to future events that are subject to risks and uncertainties as well as other factors that could cause actual results to differ materially from what is stated on today's call. These risks, uncertainties and other factors are discussed in the earnings release as well as with other documents filed by the company with the Securities and Exchange Commission. You can find these documents on our website as well.

I want to also point out that, during today's call, we will discuss some non-GAAP financial measures, which we believe will be useful in evaluating our performance. You should not consider the presentation of this additional information in isolation or as a substitute for results prepared in accordance with GAAP. We have provided reconciliations of non-GAAP to comparable GAAP financial measures in the tables accompanying the earnings release and slides. With that, let me turn it over to Jen who will be referencing **slides 3 through 5**.

Jennifer Slater
President and Chief Executive Officer

Thank you, Deb, and welcome everyone.

We delivered a strong second quarter despite a challenging macro environment which included some supply chain challenges for the industry, moderating automotive production and foreign exchange pressures. We believe our results further validate the effectiveness of our transformation actions and our focus on protecting profitability as we work to drive process improvement, institutionalize new practices and leverage the great team we have built.

Sales grew 6% driven by pricing, favorable sales mix, higher content value, new program launches, and tariff recovery.

We achieved gross margin in the quarter of 16.5% with margin expanding 330 basis points over last year.

The transformation is translating to the bottom line and delivering improved returns for our investors. Net income nearly quadrupled year-over-year to $5 million, or $1.20 per diluted share. On an adjusted basis, earnings per share grew 163% to $1.71.

During the second quarter we generated $14 million in cash from operations, bringing our year-to-date cash flow to $25 million. We have an exceptionally strong balance sheet with $99 million in cash and total debt of just $2.5 million. Our financial position gives us the flexibility to continue to invest in the business, manage through market volatility, and explore strategic opportunities.

We continue to drive actions to reduce costs and put talent in the right positions to deliver innovation and agility. During the quarter, we implemented a voluntary retirement program which, combined with other fiscal 26 restructuring actions, should generate $3.4 million in annualized savings. This layers on top of the cost reductions completed in the prior fiscal year and demonstrates our focus on operational excellence and an appropriate cost structure.

We have assembled a great team here at Strattec that is demonstrating the ability to collaborate to drive improvements across the organization. We will continue to invest in developing our employees, bringing in additional talent where needed, and providing the tools to improve processes and provide the data required for nimble decision making.

Our strong balance sheet and positive momentum provide us confidence that we can continue to execute through this cycle and create meaningful value for our shareholders. With that, I'll turn it over to Matt to walk through the financial details.

Matthew Pauli
Senior Vice President, Chief Financial Officer

Thanks, Jen, and good morning, everyone. Let me walk through the second quarter financial results in detail.

Looking at **slide 5**, sales were $137.5 million in the quarter. We have demonstrated our ability to capture accretive pricing in a disciplined way, although we will lap some of the pricing benefits in the second half of the fiscal year. We also benefited from favorable sales mix; net new program launches and higher content value including higher production volumes on the platforms we support. During the quarter we also recovered $1.3 million of tariffs costs which shows up in our net sales. As we have previously discussed, the tariff costs are recovered on a delayed basis and tend to not match up with the associated costs in any particular quarter.

All the positives we captured more than offset an overall weak automotive environment.

Sequentially, we are expecting a slight improvement in sales in the third quarter as we begin to lap pricing and follow current automotive production forecasts. On a year-over-year basis we expect the second half will be down approximately 3 to 4%.

Turning to **slide 6**, gross profit increased $5.6 million to $22.7 million in the quarter. As Jen noted, gross margin expanded 330 basis points to 16.5%, driven by multiple favorable factors. Pricing actions contributed approximately $3.1 million of the improvement. Higher production volumes provided positive leverage as we built inventories by $7 million to provide better responsiveness to our customers and to help reduce expedited logistics costs. We also captured $1.7 million in restructuring savings from our cost optimization initiatives.

These gains more than offset some headwinds. We had $1.2 million of higher labor costs in Mexico related to annual merit increases and incurred approximately $900 thousand increase in tariff costs.

We had approximately $1.6 million of negative foreign exchange impact and expect continued headwinds throughout the year. As a reminder, every 5% change in the dollar relative to the peso is an approximate $4 million annualized impact to our gross margin.

Year-to-date, we've expanded gross margin 350 basis points to 16.9%. This reflects $8 million in cumulative pricing actions, including tariff recoveries, combined with higher production volumes and $3 million in restructuring savings. Offsetting these benefits were $2.3 million in elevated Mexico labor costs and $2.1 million in unfavorable foreign exchange.

While we have much more work to be done, we believe we have raised the baseline of gross margin at the 15 to 16 percent level and are advancing toward our gross margin goal.

Moving to **slide 7**, selling, administrative and engineering expenses, or SAE, increased $2.8 million year-over-year to $17.9 million, or 13% of sales in the quarter. While the dollar increase appears significant, it's important to understand what's driving it.

We incurred $1.7 million in expenses related to our voluntary retirement program—a one-time charge. We invested an additional $0.8 million in business transformation costs, and we added $700 thousand in talent investments to strengthen our capabilities and support our growth initiatives. These investments were partially offset by $1.1 million in lower executive transition costs compared with the prior year.

Year-to-date, SAE remains controlled at 11.6% of sales, which, excluding the voluntary retirement charge, is within our expected long-term range of 10% to 11%.

Interest income grew $500 thousand on higher cash balances, reflecting our strong operating cash generation. Interest expense declined about $200 thousand on lower debt. And other income improved significantly due to the benefit of our peso hedging program.

Let's move to **slide 8**. Net income attributable to Strattec was $4.9 million for the quarter, or $1.20 per diluted share, compared with $1.3 million, or $0.32 per share, in the prior year. On an adjusted basis, net income was $7.1 million, and adjusted diluted earnings per share grew 163% year-over-year to $1.71. We are also benefitting from our cash balances. We had interest income of $885 thousand in the quarter. Our progress demonstrates that our transformation actions are flowing through to the bottom line.

Adjusted EBITDA for the quarter was $12.3 million, representing an adjusted EBITDA margin of 8.9%, compared with 6.1% in the prior year second quarter.

Year-to-date, adjusted EBITDA was $27.8 million, up 55% versus the prior year, with an adjusted EBITDA margin of 9.6%, up 290 basis points.

Now let's turn to **slide 9,** which highlights our cash position and capital flexibility.

Operating cash flow for the second quarter was $13.9 million, up 48% compared with the prior year quarter. Year-to-date, operating cash flow reached $25.2 million, up 21% versus the prior year. The improvement reflects higher net income that was somewhat offset with the investment in inventory that we made in the quarter to improve delivery times to customers. We expect the cash costs associated with restructuring and business transformation to impact the third quarter due to timing. We continue to expect to generate on an annual basis about $40 million in cash from operations.

Capital expenditures in the second quarter were $2.6 million, focused on new product programs and investments in new equipment. This resulted in free cash flow of $11.3 million for the quarter, and year-to-date free cash flow of $21 million. Year-to-date, capex was $4.1 million and we expect that capex for fiscal 2026 will be less than $10 million.

We ended the quarter with a very healthy cash position of $99 million. We paid down another $2.5 million of debt in the quarter. Total debt, which is related to our joint venture, is just $2.5 million, down from $8 million at the end of the prior fiscal year.

We are consistent with our capital allocation priorities. First, we are prioritizing investments to support organic growth and new customer programs. Second, we are investing in process modernization and automation initiatives which we expect to drive efficiencies and improve our manufacturing footprint. Third, we're preserving financial flexibility as we navigate the uncertain automotive market. And finally, we're evaluating M&A as a potential lever for longer-term growth.

If you turn to **Slide 10**, I'll hand it back to Jen to review the conditions in the automotive industry and the actions we are taking.

Jennifer Slater
President and Chief Executive Officer

Thanks, Matt. While North American automotive production is not looking as challenging as originally expected at the beginning of fiscal 26, industry forecasts still suggest a flat to moderate decline. While we will have modest benefits from program launches and being on favored platforms this fiscal year, we are still subject to OEM production rates.

To sum up, we are delivering on the transformation of Strattec. We've expanded margins significantly, nearly tripled net income, and grown adjusted EBITDA by 55% year-to-date. We're building a stronger business with improved earnings power. We have a great balance sheet, giving us the capital to invest and the flexibility to manage through cycles.

While there are a number of obstacles we have yet to overcome, we believe our strategic focus on deepening our customer relationships in engineered access solutions along with striving for operational excellence should enable sustainable, profitable growth. We also have the opportunity to expand our customer set within North America by leveraging our technical expertise. We believe the talent we have invested in and the organizational muscle we are building are making meaningful contributions that are critical to the future of Strattec.

We have good momentum heading into the second half of fiscal 2026, and we're confident in the path that we are on.

With that, operator, we're ready to open the line for questions.

Question and Answer

Operator

Thank you. [Operator Instructions] Thank you. Our first question comes from John Franzreb with Sidoti & Company. Please proceed.

John Franzreb

Good morning, everyone, and congratulations on another great quarter.

I actually would like to start with the just-finished period. Jennifer, I know there were concerns that supply chain disruptions might be problematic. I'm curious, was there actual revenue pushed from Q2 into Q3, or did your customers pretty much work around it? And it was pretty much a non-issue?

Jennifer Slater

I think there were two things that we talked about. One was the fire at an aluminum supplier for some of our customers. There was some slight impact from that on certain platforms that customers are looking to make up for the full year. And then the other one was the chip challenge. And I would say that customers worked with suppliers to get through that with minimal impact to sales in the quarter.

John Franzreb

It always seems to be a chip challenge out there. Regarding the selling and administrative expenses in the second half, with the change in compensation, with new people coming on board with early retirement plan; how should we think about that line item? Is that going to be closer to the second quarter's 13%, or is it more of the first half's 11.8%, 11.6%? How should we think about how that line item plays out for the year?

Jennifer Slater

I think maybe I'll start with a little bit of context on how we're evaluating that investment, and then Matt can talk a little bit more on the target. This is an area, John, we're continuously looking at. Where do we need to invest in continuing the progress on the transformation? There's a lot of puts and takes in there. But we also want to make sure that we're not starving the long term, for where we need to be with the business, as we think through the investment. But I think, you know, we've set where we think the target of the business is, and that's where we're continuing to work through. And I'll let Matt answer more specifically.

Matthew Pauli

Yes, we still expect it to be in the 10 to 11% in the back half of the year, John. We've talked about merit, especially in Mexico in the past. What I think we'll see going forward on merit, is it'll be a little bit less of an increase than what we've had to do historically. I think two years ago it was kind of 20%, 12% this past year, but it'll be a little bit less than that on a go-forward basis. So, expect 10 to 11% from an SAE perspective in the back half of the year.

John Franzreb

Got it. Thank you, Matt. Going into $3.4 million in savings from the early retirement plan. When does that hit the bottom line is that immediately in the third quarter? I saw that you took the $1.7 million, you know, against that. How does that play out?

Matthew Pauli

Just to clarify, the $3.4 million is the annual benefit for the restructuring actions and the voluntary retirement program that we did in fiscal 26. So, we saw only saw about 400,000 of a benefit in the current quarter, and it will kind of get fully phased in roughly around 800,000 a quarter by the time we get to the fourth quarter.

John Franzreb

Perfect. I guess one more question and I'll get back into queue. Regarding the free cash flow, you've had a great bunch of quarters, what's the pushback that's going to draw down the cash flow? It sounds almost like there's an inventory build going on, but I'm not sure if I just misheard that in the presentation.

Matthew Pauli

I think we've talked about it in the past. We were intentionally building finished good inventories, in the quarter just to improve our service delivery to our customers. So that was a headwind in the quarter. But also, you know, some of the restructuring costs and the business transformation costs that we expensed in the second quarter will impact cash flow in the third quarter.

John Franzreb

Great. All right, Matt, thanks a lot. I'll get back in the queue.

Operator

Our next question is from Brian Sponheimer with Gabelli Funds LLC. Please proceed.

Brian Sponheimer

Hey good morning, everyone. Could you just talk a little bit about some of the conversations you're having with potential new customers in North America? You mentioned that as a source of growth. Obviously, that's not a fiscal 26 or potentially fiscal 27 item, but maybe just where some of those conversations are going on and what products are centering on.

Jennifer Slater

We are focused on our access products and our digital key as we are talking to our existing and prospective customers. As you know, Brian, the sales cycle in automotive is a long sales cycle. So, starting the discussions right now to get our customers comfortable with our product portfolio, the value we can provide, and lining those up to the timing of their model year launches. The very earliest it would be is 2029, but it's more likely to be longer term as they're going through their product plans, qualifying us as a supplier and then spec'ing those into the platforms. Once we are spec'd into the platforms, we are on for the life of the platform, which is typically 5 to 7 years.

Brian Sponheimer

Okay. One other one from me: Tesla had a very high-profile issue with the door handle that you're not on. But does this impact you from a technology perspective on any prospective platforms that you had coming out in the next couple of years with a similar mechanism on proximity handles?

Jennifer Slater

For door handles it doesn't impact us for what we plan for the future. But I would say that the benefit to us, as we provide mechanical locking mechanisms as well, is it's just reinforcing that while technology is changing, there still is a need for a secondary mechanical locking mechanism to enter into vehicles. I see this as continued strength for our product offerings to the customers.

Brian Sponheimer

All right. Thank you very much.

John Franzreb

Hi, Jennifer, I'd be remiss not to ask this question every quarter. It's regarding your product review. Can you give us any kind of update of what you're finding as you go through a product line by product line review of the company's offerings?

Jennifer Slater

It's a good question, John. We talked about earlier in the year that we did have a product line, which was our switch business, that we deprioritized because while we had some good technology there, it wasn't the right fit from a profit and the value that we could supply to our customers. We still are heavily focused on our power access products, which is our drive units, our latching mechanisms, door handles, as well as our digital key technology, which is the next generation technology of a traditional key fob. So, when I talk about digital key, it's the actual key fobs next generation technology.

John Franzreb

Got it. And just a point of clarification, Matt. I think you said that you expect revenue to be up 3 to 4% in the second half. I'm not sure if you're referencing year over year or sequentially.

Matthew Pauli

Just to clarify, the expectation is that it will be down 3 to 4% on a year-over-year basis.

John Franzreb

Okay, thank you for that. I'm glad I asked the question. Thank you for taking my follow-ups.

Operator

There are no further questions at this time, so this does conclude today's teleconference. You may disconnect your lines at this time and thank you for your participation.