

A person in a red jacket stands in a cave, illuminated by a bright blue light source. The cave walls are dark and textured, and the floor is covered in rocks. The overall atmosphere is mysterious and dramatic.

*corbin*

# Inside The Buy-side<sup>®</sup>

Q2'21 Industrial Sentiment Survey

July 22, 2021

# Inside The Buy-side® Q2'21 Industrial Sentiment Survey

For 13 years, we have surveyed global investors quarterly on the equity markets, world economies and business climate. At the start of every earnings season, we publish our leading-edge research, *Inside The Buy-side Industrial Sentiment Survey*, which captures real-time Voice of Investor® sentiment and trends.

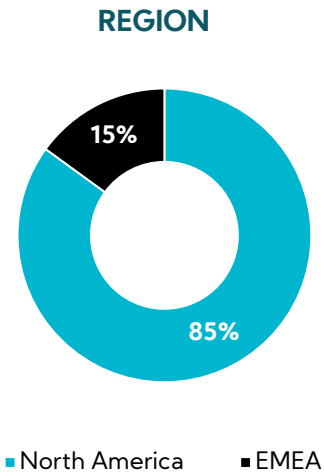
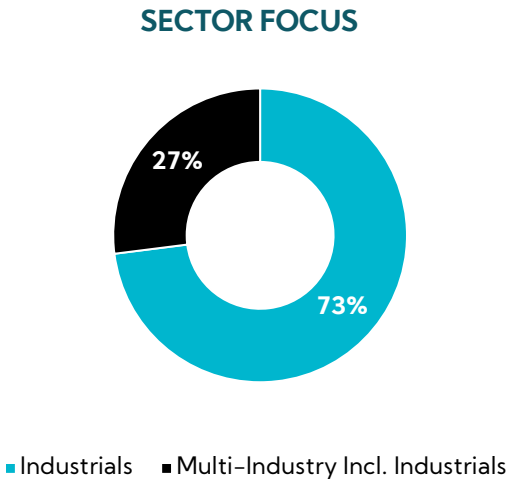
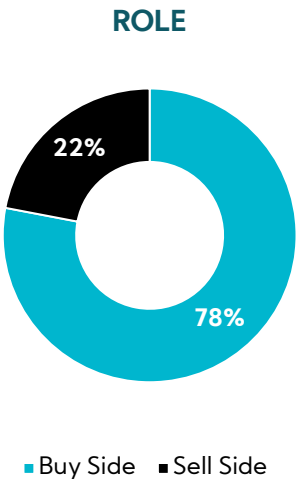
Leveraging our deep understanding of capital markets, cutting-edge technology and best practice knowledge, our research demonstrates the value we add by remaining at the forefront of global market trends, investor sentiment and effective communication strategies.

**Survey Scope:** 37 sector-dedicated investors and analysts globally; buy side firms manage ~\$3.9 trillion in assets, including ~\$429 billion invested in Industrials

**Survey Timeframe:** June 15 – July 15, 2021

Issue: 25  
Date: July 22, 2021

MARKET PERFORMANCE	Q2'21	Q2'20
DJIA	4.1%	17.8%
NASDAQ	7.6%	30.6%
S&P 500	6.9%	20.0%
S&P 500 Industrial	7.2%	16.4%
Russell 2000	2.5%	25.0%



# Word Cloud: Frequency of Occurrence

Visual representation of investment community focus areas, trends in frequency of word occurrence and underlying tone

## Exuberant Growth Expectations Saddled by Inflation and Supply Concerns



TOP MENTIONS	Q3'20	Q4'20	Q1'21	Q2'21	Q/Q
Cost	6	10	13	27	↑ 14
Inflation	-	3	14	24	↑ 10
Growth	6	18	19	14	↓ 5
Margins	-	6	3	14	↑ 11
Supply Chain	5	5	14	14	UNCH

# Despite Significant Spike in Inflation Concerns, Expectations for Top Line Blowouts this Quarter and Continued Growth in Back Half of 2021

## Universal Expectations for Sequential Revenue Growth – a Survey First – and EPS Beats Projected, Too

- 96% of surveyed investors and analysts describe management tone as *Neutral to Bullish* or *Bullish*, another record, surpassing the previous high set last quarter
- 100% expect revenue to *Improve* sequentially, the first ever unanimous consensus registered
- 71% believe earnings will *Improve* QoQ and 65% anticipate Q2 beats, up from 57%
- 85% expect companies that issue revenue guidance to raise, and 79% expect the same for EPS
- Oil & Gas Markets, Unemployment Rate and Global Capex expected to see the most improvement over the next six months

## Margins Take Center Stage – Despite Rapid Cost Inflation, Investors Anticipate Margins Will Remain Stable This Quarter, Buoyed by Double-Digit Growth

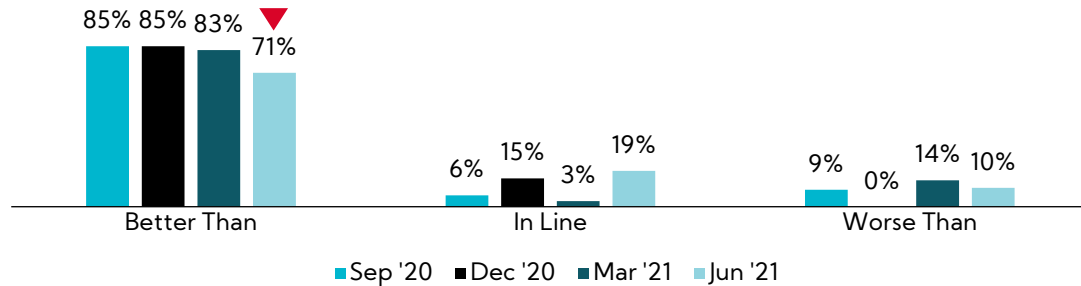
- 88% identify inflation as the most significant concern, up from 55% last quarter
- 46% identify margins as the leading topic for executives to address on upcoming earnings calls, nearly 3x higher than last quarter, related to and followed by inflation (38%)
- 56% expect margins to *Stay the Same* sequentially, up from 39% last quarter; fewer than 15% expect margins to *Worsen*
- 65% *do not* expect companies that guide on margins to raise

## Views on Capital Allocation Support Growth Mindset while Conservatism on Debt Levels Continues to Ease

- 63% expect FCF to *Improve* sequentially, up from 46% last quarter
- 84% prefer reinvestment as the top use of cash, followed by M&A at 38%, up from 28% last quarter
- 73% identify *Consolidation Story* as the most compelling investment theme at this time
- 91% are in favor of bolt-ons and 67% are comfortable with companies leveraging up to 4–4.5x for compelling acquisitions, notably less conservative than the 3–3.5x last quarter
- 38% encourage executives to address capital allocation on upcoming earnings calls, a top three area of focus

# Continued Sequential Strength and Earnings Beats Expected amid Stronger than Anticipated Demand

Q2'21 EARNINGS EXPECTATIONS VS. PRIOR QUARTER



## Better Than

*"Strong macro data, reopening of the U.S. post-COVID."* **Buy Side, Industrials, N. America**

*"Earnings better be higher than last quarter. Last quarter saw big beats. This quarter will be more in line, slight beats."* **Buy Side, Industrials, N. America**

*"Industrials are largely expected to generate pretty positive outcomes for Q2. We would be looking much further beyond that but generally, the trends have been pretty good through the first half of the year."* **Buy Side, Industrials, N. America**

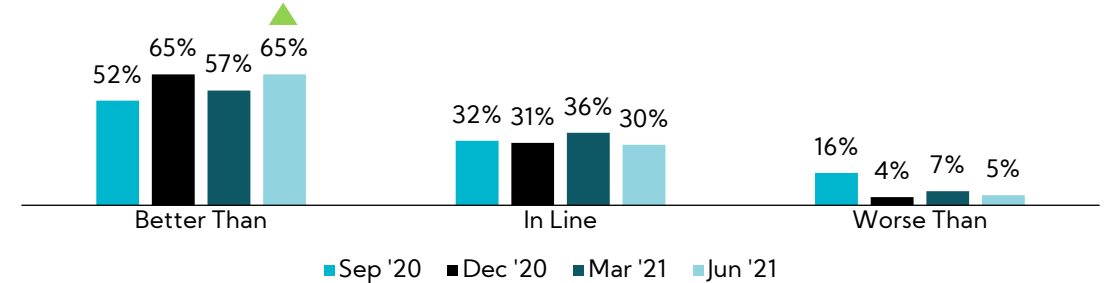
*"Seasonality and pandemic recovery."* **Buy Side, Generalist, N. America**

*"Stronger demand than initially expected at better price points."* **Sell Side, Industrials, N. America**

*"Reacceleration production ramp is more than offset rising input costs, logistics and labor shortages...so far, as breadth of revenue expansion broadens to virtually all markets."* **Sell Side, Industrials, N. America**

*"Overall rebound."* **Buy Side, Generalist, Europe**

Q2'21 EARNINGS EXPECTATIONS VS. CONSENSUS



## In Line

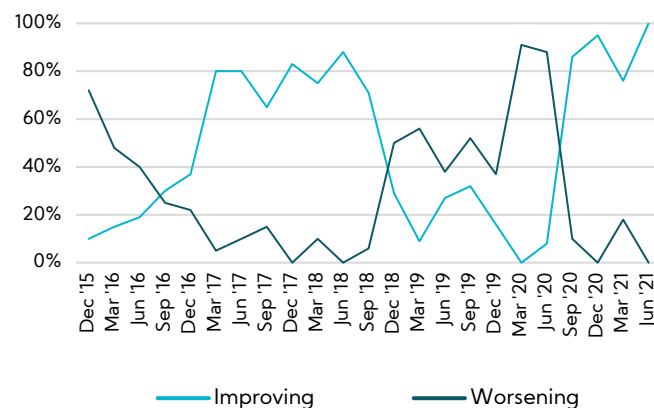
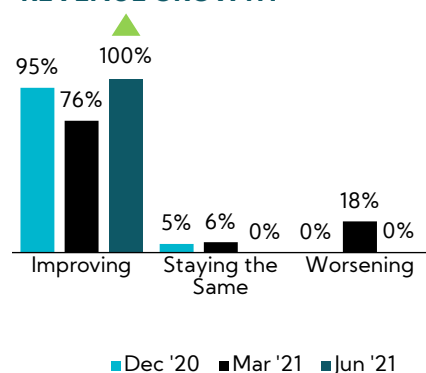
*"Q2 will be strong against a very easy COVID-affected prior year comparison."* **Buy Side, Industrials, N. America**

*"No near-term momentum/positive catalysts since Q1 – drivers are understood – revenue probably better but pressure on costs nets it out."* **Buy Side, Industrials, N. America**

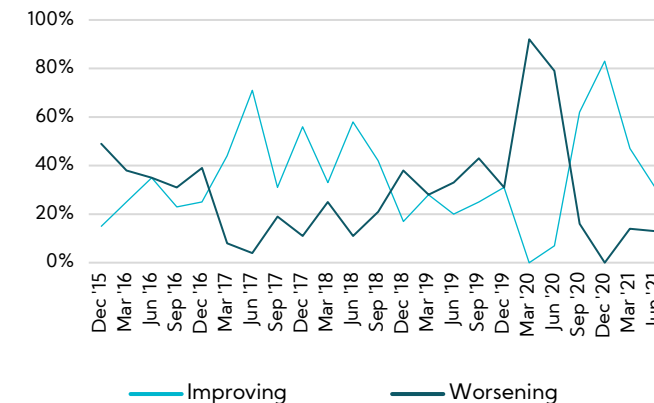
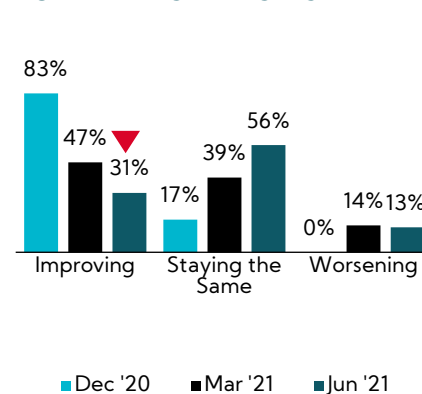
*"It will be an okay quarter. Maybe Q3 is going to be the biggest quarter and the reopening will have the biggest impact. Maybe year-over-year Q2 is going to be okay but I am not sure it is going to be the big quarter that some investors are looking at. It might be an in-line quarter."* **Buy Side, Industrials, N. America**

# Highest Level of Revenue Growth Optimism Ever Recorded as Expectations for Margin Expansion Take a Breather amid Pervasive Cost Inflation

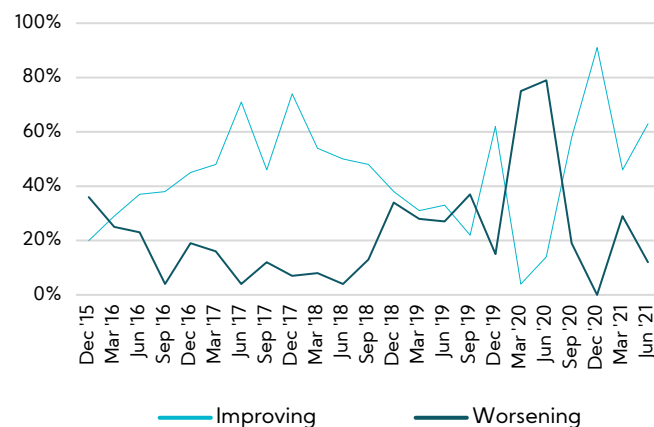
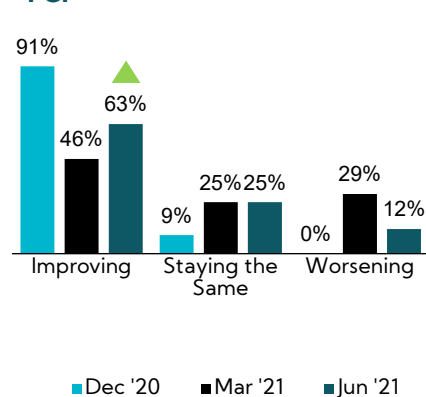
## REVENUE GROWTH



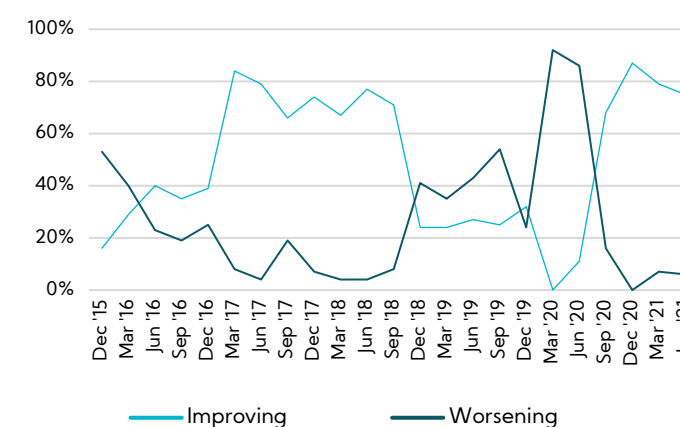
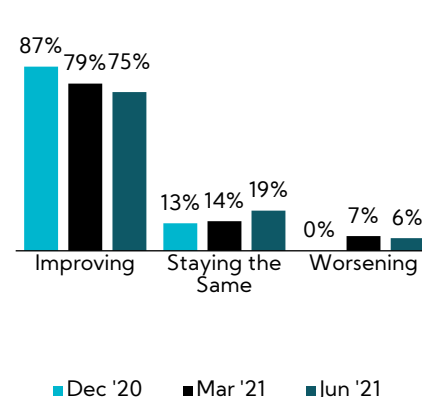
## OPERATING MARGINS



## FCF

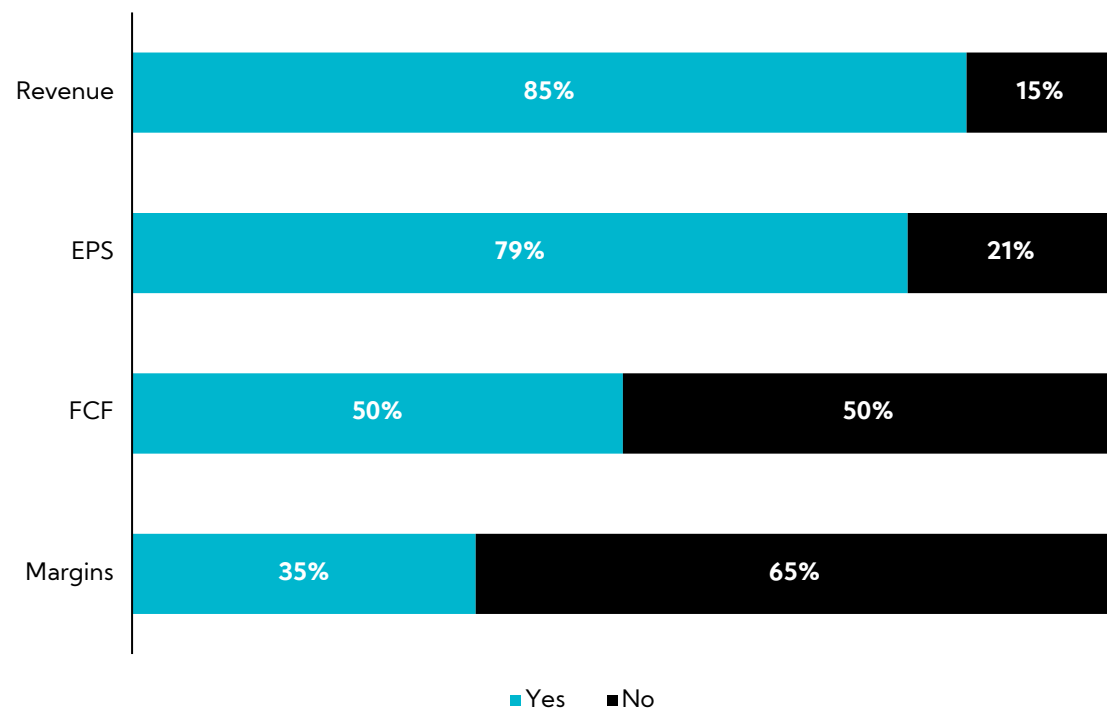


## EPS



# Majority Expect Revenue and EPS Guidance Raises this Quarter (Again) But Recognize Upsized Margins Are Unlikely

## EXPECTATION FOR INDUSTRIAL COMPANIES TO RAISE ANNUAL GUIDANCE



*"Demand is strong but costs are rising."* Buy Side, Industrials, N. America

*"Cost inflation and supply chain constraints could dampen margin expansion."* Buy Side, Industrials, N. America

*"Cost pressure and delays could hold back margins but directly revenues and EPS will be growing."* Buy Side, Industrials, N. America

*"On average, I am expecting them to rise annual guidance. Maybe not margins but I expect most companies to raise revenue and EPS status and FCF to the extent they guide to that."* Buy Side, Industrials, N. America

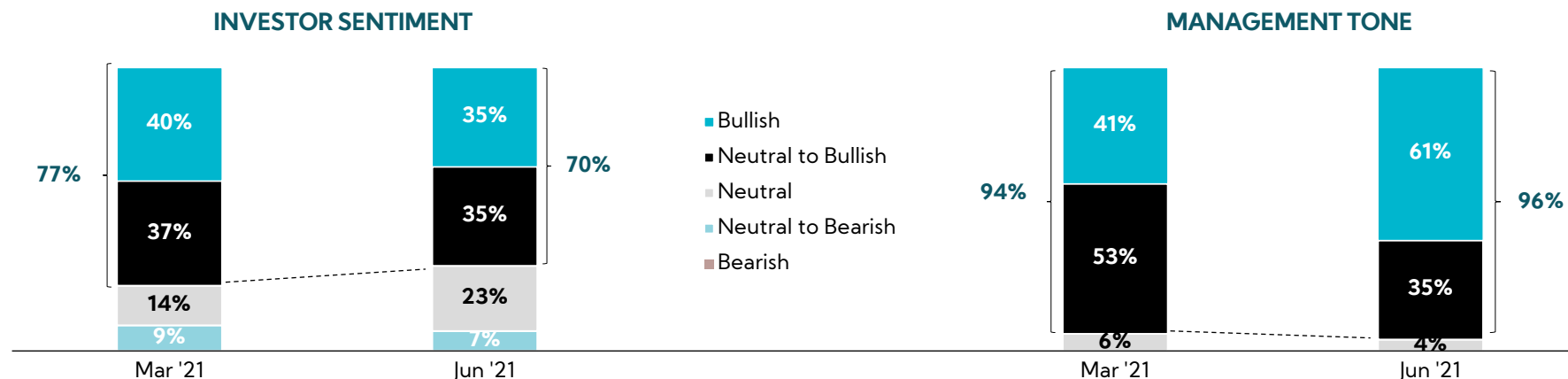
*"Inflation expectations and low yields may temper more specific H2 guidance."* Buy Side, Generalist, N. America

*"We have not adjusted numbers yet, so we have to work through it. I am mixed. This is a Tier 1 discussion. It is a mix of maintaining to raising guidance depending on specific companies. Where you are raising guidance, it is better content and a better margin trajectory versus balancing out potentially sustained or less bad supply chain headwinds in the back half of the year but not as meaningful a snapback as some had hoped."* Sell Side, Industrials, N. America

*"Management will hold optimism about several price hikes gaining traction in their pocket for 2H'21 but notably better-than-expected revenues will force them to lift sales guidance for 2021; FCF should be good but working capital usage is likely to be higher than normal due to supply chain disruption and accelerating pace of sales and billings at end of 2Q21 vs. start of 2Q21."* Sell Side, Industrials, N. America

*"Yes, everybody is going to raise guidance this quarter and if somebody does not raise guidance this quarter, they are going to be an anomaly. That is the expectation for everybody, not just my expectation."* Sell Side, Industrials, N. America

# Perceived Bullish Management Tone Registers at Record Highs While Investor Bullishness Recedes



## Bullish

"End markets in the early stages of recovery." **Buy Side, Industrials, N. America**

"Growth is accelerating. Risks include supply chain constraints and cost inflation." **Buy Side, Industrials, N. America**

"It is positive. A lot of companies in the industrial sector are tied to the economy and they are looking at fewer restrictions around COVID. All those things are positive for the reopening and they are seeing a lot of demand. With management, sentiment is bullish whenever I talk with them. Everything seems good." **Buy Side, Industrials, N. America**

"Strong demand at higher price points." **Sell Side, Industrials, N. America**

## Neutral to Bullish

"Management is largely positive but think stocks factor all the positive. So, near-term risks to stock relative to expectations." **Buy Side, Industrials, N. America**

"End market demand is strong; companies are struggling to execute because of supply chain challenges and inflation pressure but the demand side looks solid. Management is also neutral to bullish. They see healthy underlying demand but they struggle executing." **Buy Side, Industrials, N. America**

"I am bullish on their business prospects and neutral on their valuation. With management, their tone is upbeat and excited about the potential growth from all these government initiatives and people getting back to work and what that does for their business, plus the greening of the economy is a very strong positive impact for this group." **Buy Side, Industrials, N. America**

"In the infrastructure space, there is huge spending, which is positive as we are still in the midst of a recovery. In a lot of cases, we have had a lot of price appreciation for shares. That is a bit of an offset. Otherwise, I am quite bullish." **Buy Side, Generalist, N. America**

"Concerns about slower growth in China balanced by supply constraints." **Sell Side, Industrials, N. America**

## Neutral

"We are mixed. It is about second derivative improvement flattening and cost coming back and capital deployment opportunities being more balanced. I would describe management as bullish." **Buy Side, Industrials, N. America**

"The valuations on most names are high, so that keeps me from being bullish. For management, most people are bullish on their own business. A lot of that has to do with the recovery of businesses across the board post-COVID and inflation being driven by a lot of the commodities, which feeds into a lot of the industrial businesses, so that drives most people to be bullish." **Buy Side, Industrials, N. America**

"Expectations are pricing a lot in of improvement – probably not enough sales growth and perhaps a bit too optimistic on margins and FCF generation." **Sell Side, Industrials, N. America**



46% (↑ 30pts QoQ)  
Margins

38% (↑ 13pts)  
Inflation

38% (↑ 5pts)  
Capital Allocation

33% (↓ 47pts)  
Growth

25% (↑ 25pts)  
Labor Shortages

## Topics of Interest for Upcoming Earnings Calls

*With growth a slam dunk this quarter and inflation everywhere you turn, margins now the leading area of focus on upcoming calls*

### Views from N. America

*"Sustainability of recovery, margins, M&A." Buy Side, Industrials*

*"It depends on which companies but maybe the continuity, recovery and reopening. Are they as strong as we expect, are they starting to look at it or is that too much of an expectation, is that going to be materialized? Also, how is inflation impacting them? Will they do better revenues versus their costs? Will there be a lag? Trying to understand all of that and what the impact of inflation is." Buy Side, Industrials*

*"I like executive leadership to remind investors what their game plan is and then speak to the things they are doing today to facilitate their long-term objections. A quick reminder of who we are and what we do and let us talk about what we are doing today to continue to enhance and create value. If they do that in the context of the recent set of results, that is always additive. 'One of our key corporate initiatives is to expand margin. Look at the recent quarter, June. We have expanded margins in three of our four divisions. Expect more of that from us, we hope, and here is how we are going to do it.' We want to see people with a plan and simplified articulation of the steps they are taking to create sustainable value for shareholders." Buy Side, Industrials*

*"Cost inflation, pricing, supply chain." Buy Side, Industrials*

*"Organic growth trends, margin preservation/improvement in an inflationary world, internal investment opportunities." Buy Side, Industrials*

*"What is the ability to pass through price to mitigate cost inflation? Are customer capex decisions improving? How far below normal are customer and channel inventories?" Buy Side, Industrials*

*"It is always organic growth, M&A, capital allocation, margins." Buy Side, Industrials*

*"Materials and labor cost increases." Buy Side, Industrials*

*"Labor market shortages, outlook for oil prices, capacity growth." Sell Side, Industrials*

*"Labor shortage/hiring adequacy, runway to grow organically, oath to not repurchase shares unless trading <9X EBITDA." Sell Side, Industrials*

*"Growth, margins, cost control." Sell Side, Industrials*

# Top Concerns from around the Globe

*9 in every 10 industrial investors cites inflation as a top concern*

88% (↑ 33pts)	Inflation	56% (↑ 14pts)	COVID-19 delta variant	26% (↑ 9pts)	Supply issues (disruption, constraints)
26% (↑ 14pts)	Consumer health	20% (↓ 9pts)	Valuations	18% (↓ 3pts)	Interest rates

## Views from N. America

*"Supply chains; raw materials; another wave of the delta variant." Buy Side, Industrials*

*"Cost inflation; supply chain constraints; COVID variants." Buy Side, Industrials*

*"Inflation pressure; supply chain bottlenecks; impact on valuation if rates rise." Buy Side, Industrials*

*"Peak margins; 2022 revenue growth; Fed." Buy Side, Industrials*

*"Inflation; cost increases; COVID incidence outside the U.S." Buy Side, Industrials*

*"Inflation; consumer health." Buy Side, Generalist*

*"Inflation; I expect inflation will rise significantly in the back half of 2021." Buy Side, Generalist*

*"Pandemic-related shutdowns [and] the constant starting and stopping; declines in personal spending on travel after Labor Day; the economy in 2H'21." Sell Side, Industrials*

*"2Q'21 super ramp could have to tap on the brakes (maybe hard) if delta variant spurs resurgence in need for increased restrictions; younger population should be required to get vaccinated for school, college, sports, etc.; the longer inflation resurgence expectations remain muted, the more likelihood industrial valuations could compress." Sell Side, Industrials*

*"Labor inflation; tough compares into 2022; price/cost." Sell Side, Industrials*

*"Interest rate increases; another COVID-19 wave; China." Sell Side, Industrials*

## Views from EMEA and APAC

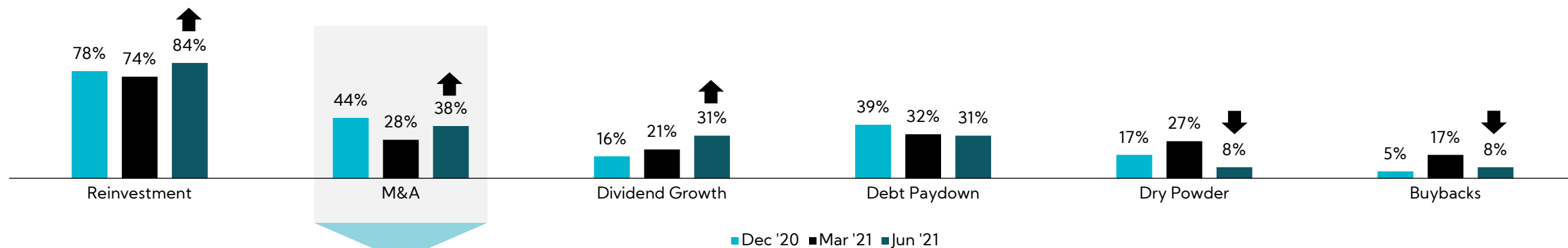
*"Consumer behavior; inflation; interest rates." Buy Side, Generalist*

# Reinvestment Overwhelmingly Favored, Followed by M&A

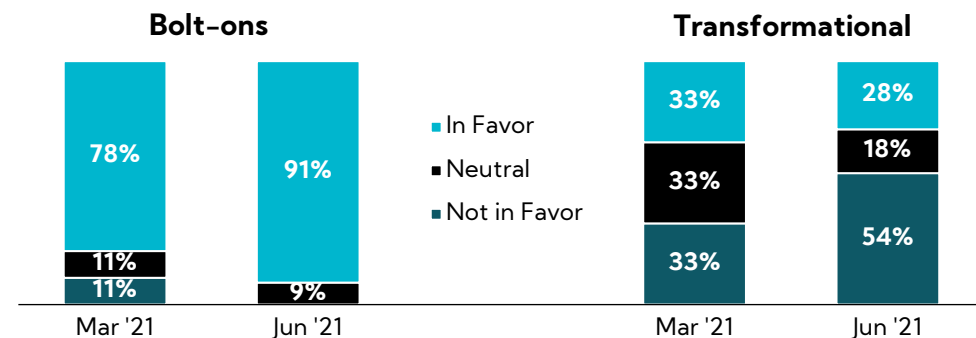
*Investors increasingly less conservative regarding companies leveraging up for M&A amid strong acquisition activity globally*

## PREFERRED USES OF CASH FOR INDUSTRIALS

In Descending Order of Top Two Preferences

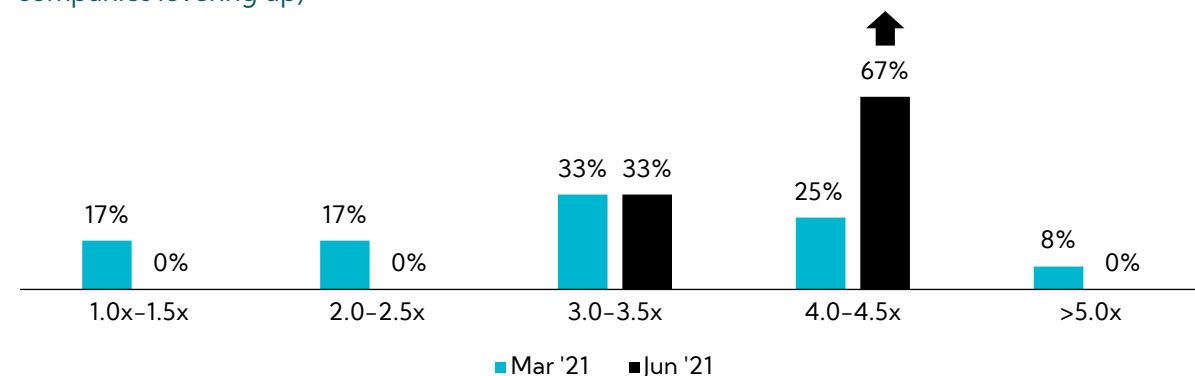


## M&A PREFERENCES



## COMFORT LEVEL WITH LEVERAGE FOR COMPANIES FUNDING M&A WITH DEBT

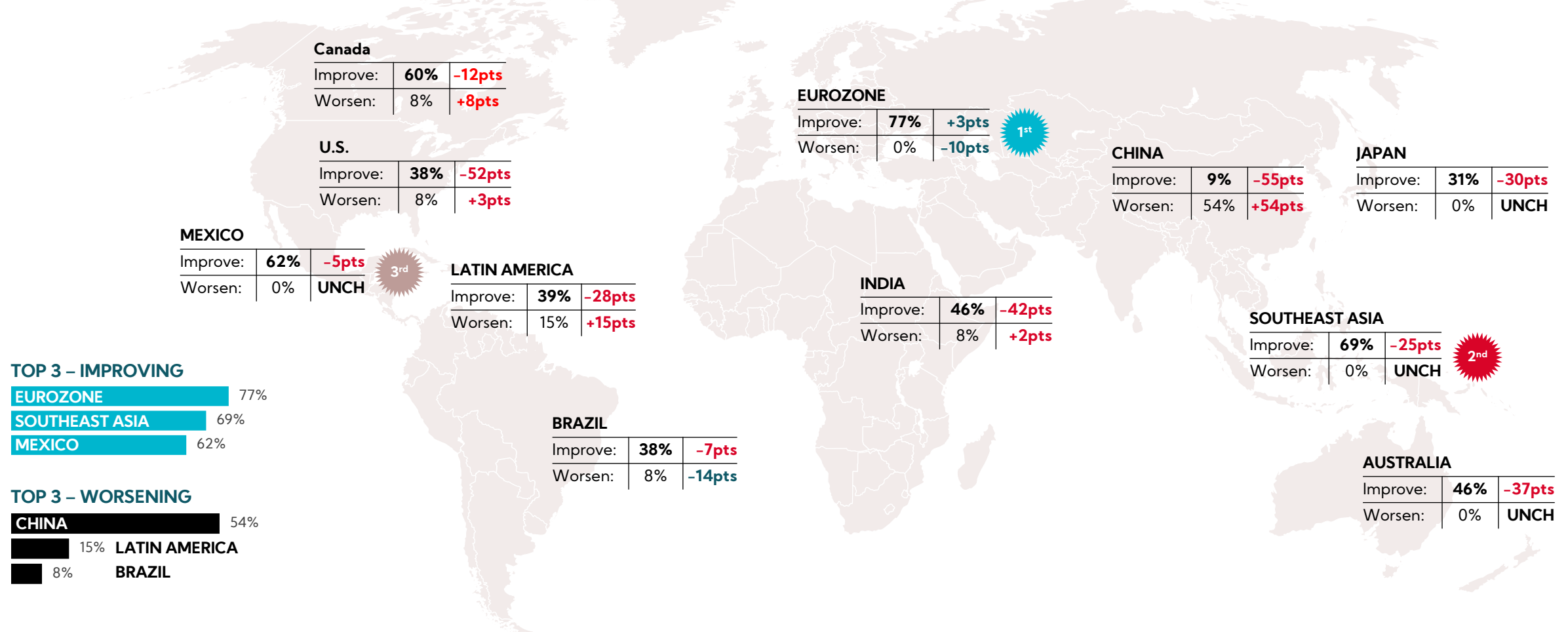
(Assuming a compelling transaction, the level to which investors would be comfortable companies leveraging up)



# After Continued Improvement Was Expected Globally Last Quarter, Exuberance Stalls amid Growing Concerns, Including Delta Variant Strike

*Eurozone expected to see the most significant improvement over the next six months while China sees largest degradation in confidence*

## GLOBAL ECONOMY EXPECTATIONS OVER THE NEXT SIX MONTHS

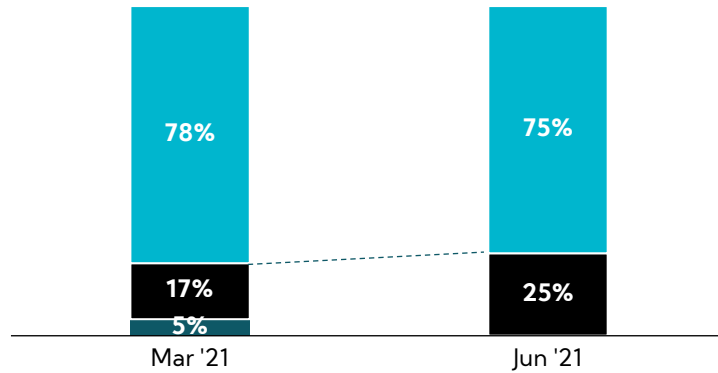


# Views on Key Economic Indicators Over the Next Six Months

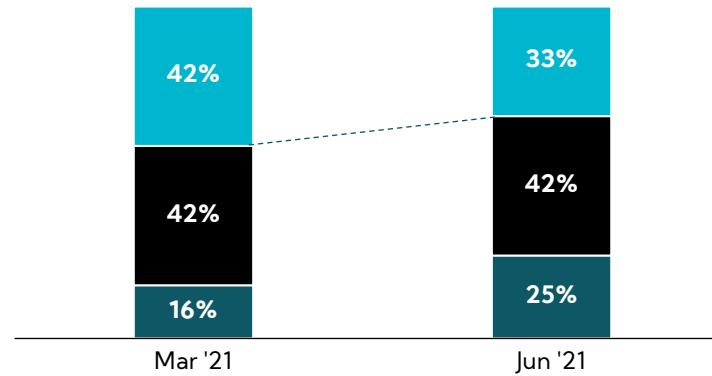
*Forecasts are for Improving Oil & Gas markets, Unemployment Rate and Global Capex while Consumer Confidence expected to take a hit*

■ Improving ■ Staying the Same ■ Worsening

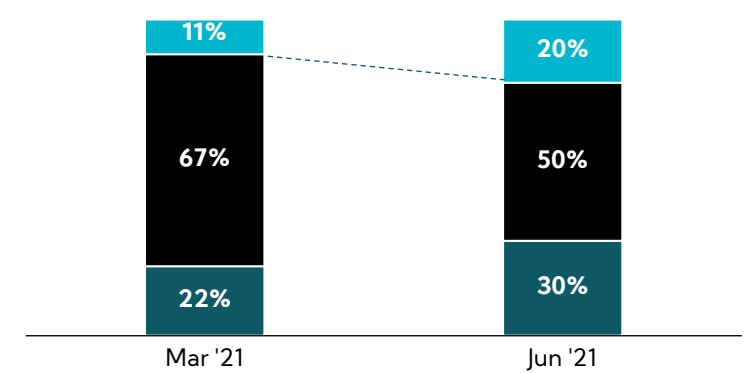
GLOBAL CAPEX



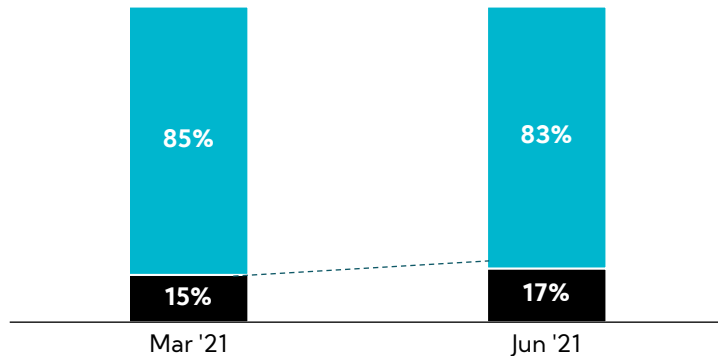
GLOBAL PMI



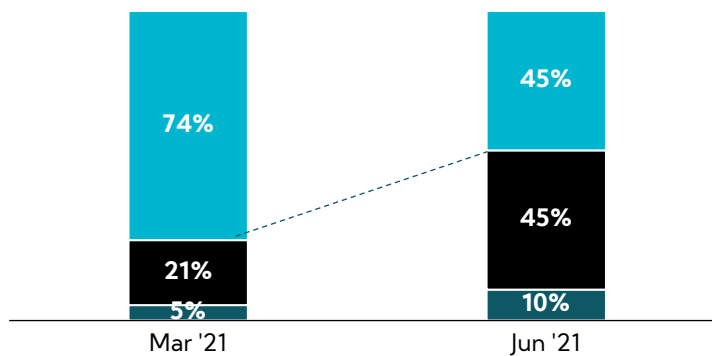
FX HEADWINDS



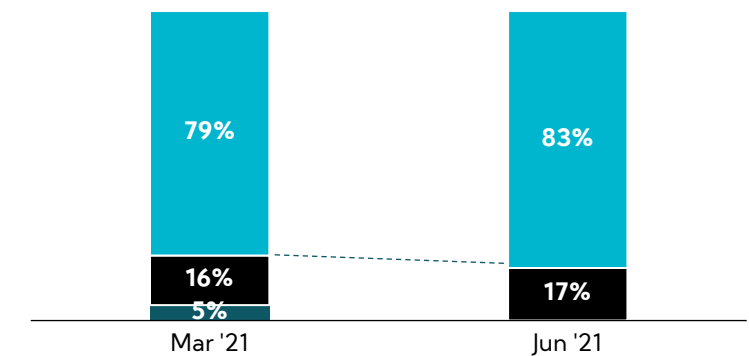
OIL & GAS MARKETS



U.S. CONSUMER CONFIDENCE

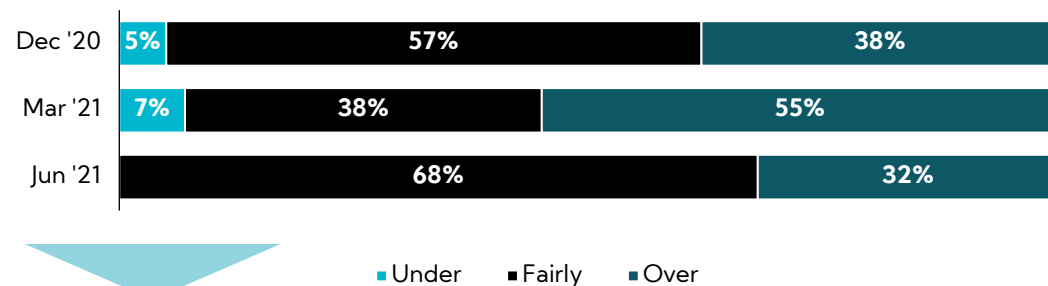


U.S. UNEMPLOYMENT RATE

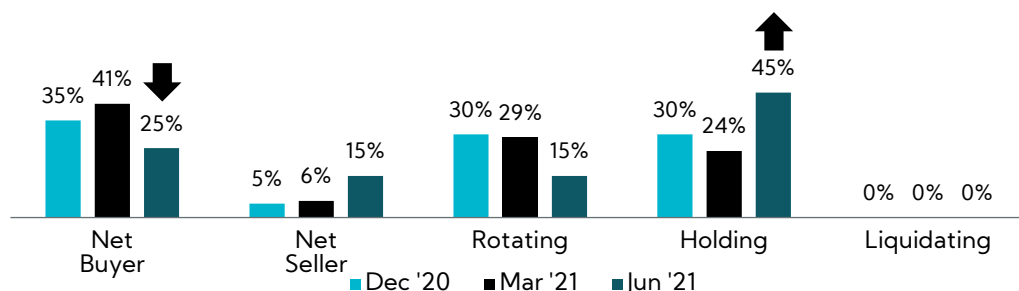


# Industrials Now Considered More Fairly Valued as Investors Move from Buy to Hold Strategy

## GLOBAL INDUSTRIAL VALUATIONS



## QoQ INVESTMENT TRENDS



### Fairly

"Above historical ranges but in line with the overall market." **Buy Side, Industrials, N. America**

"A lot of companies are fairly valued. I do not know if I can say overvalued. It is hard to tell but a lot of companies have had a huge run since a year ago, after the big crash. A lot of companies did really well and for companies like aviation or others that were more impacted, recently they had huge moves. It is hard to find good opportunities out there." **Buy Side, Industrials, N. America**

"They are more or less reasonable. It is mixed. Some things are good; some things are bad." **Buy Side, Industrials, N. America**

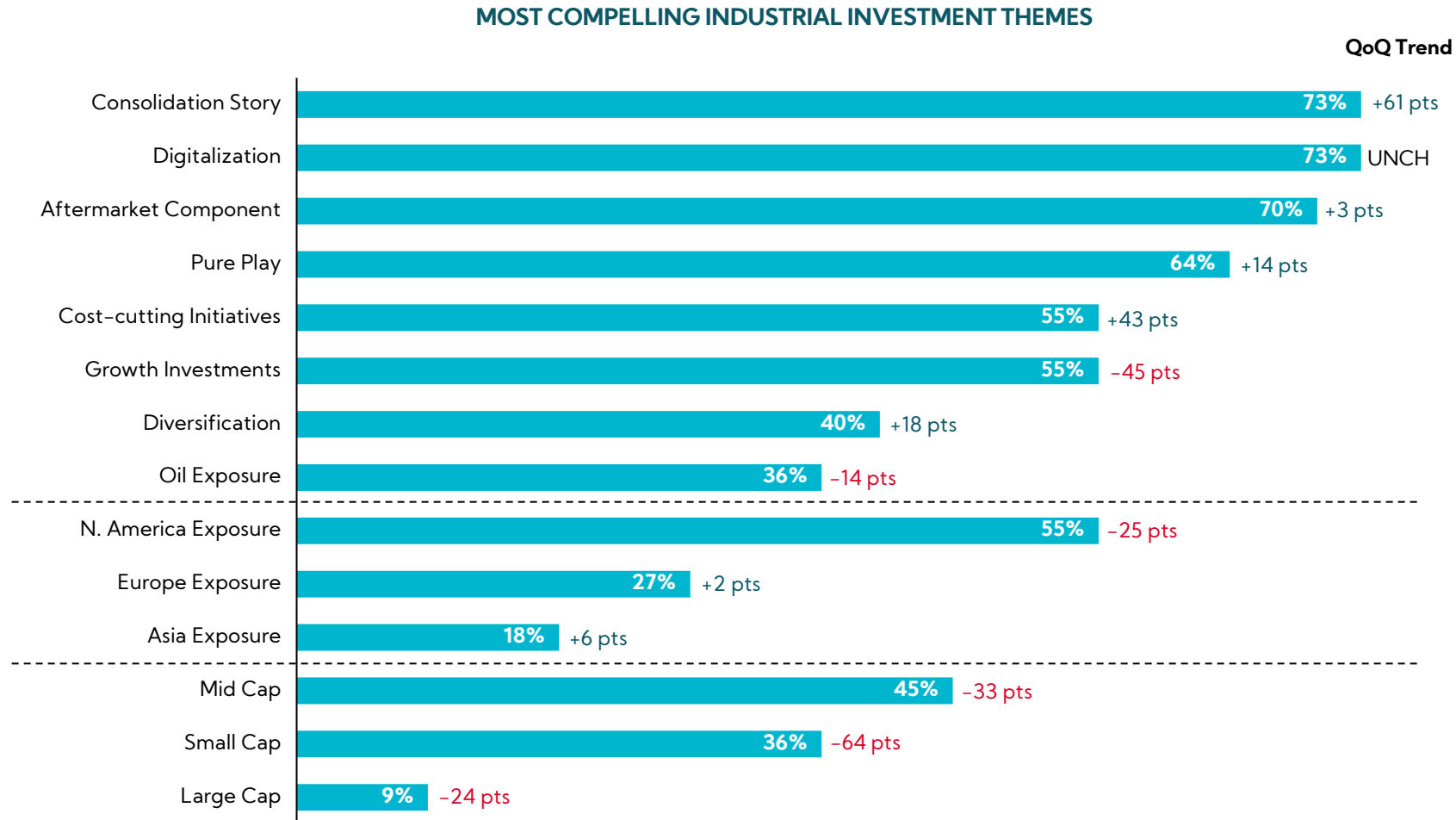
"A lot of them are fair to overvalued. They are reflective of the more bullish sentiment in the market." **Buy Side, Industrials, N. America**

### Over

"Stocks in my industry are trading on 2023 earnings, which is a little far away. On 2021 earnings, they are overvalued." **Sell Side, Industrials, N. America**

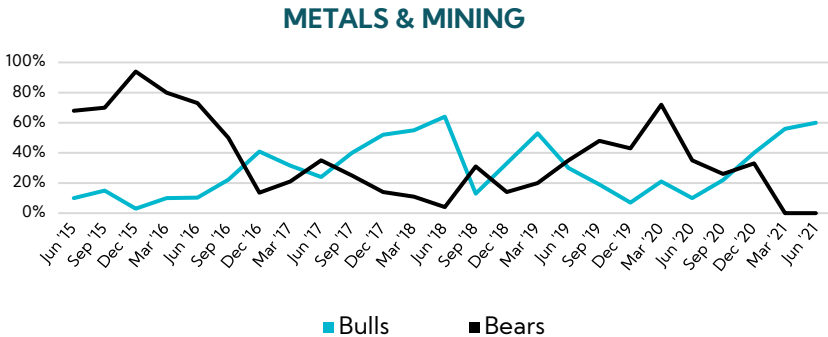
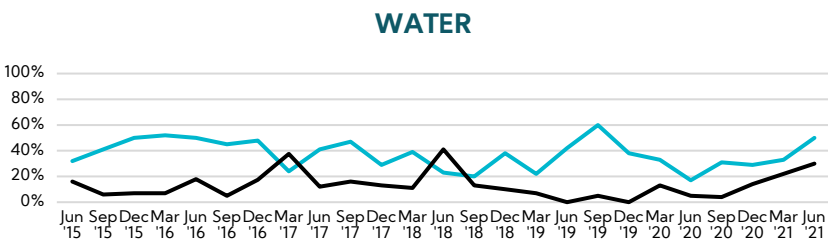
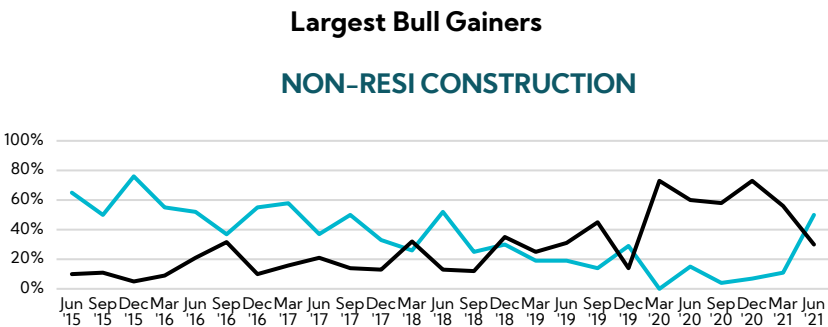
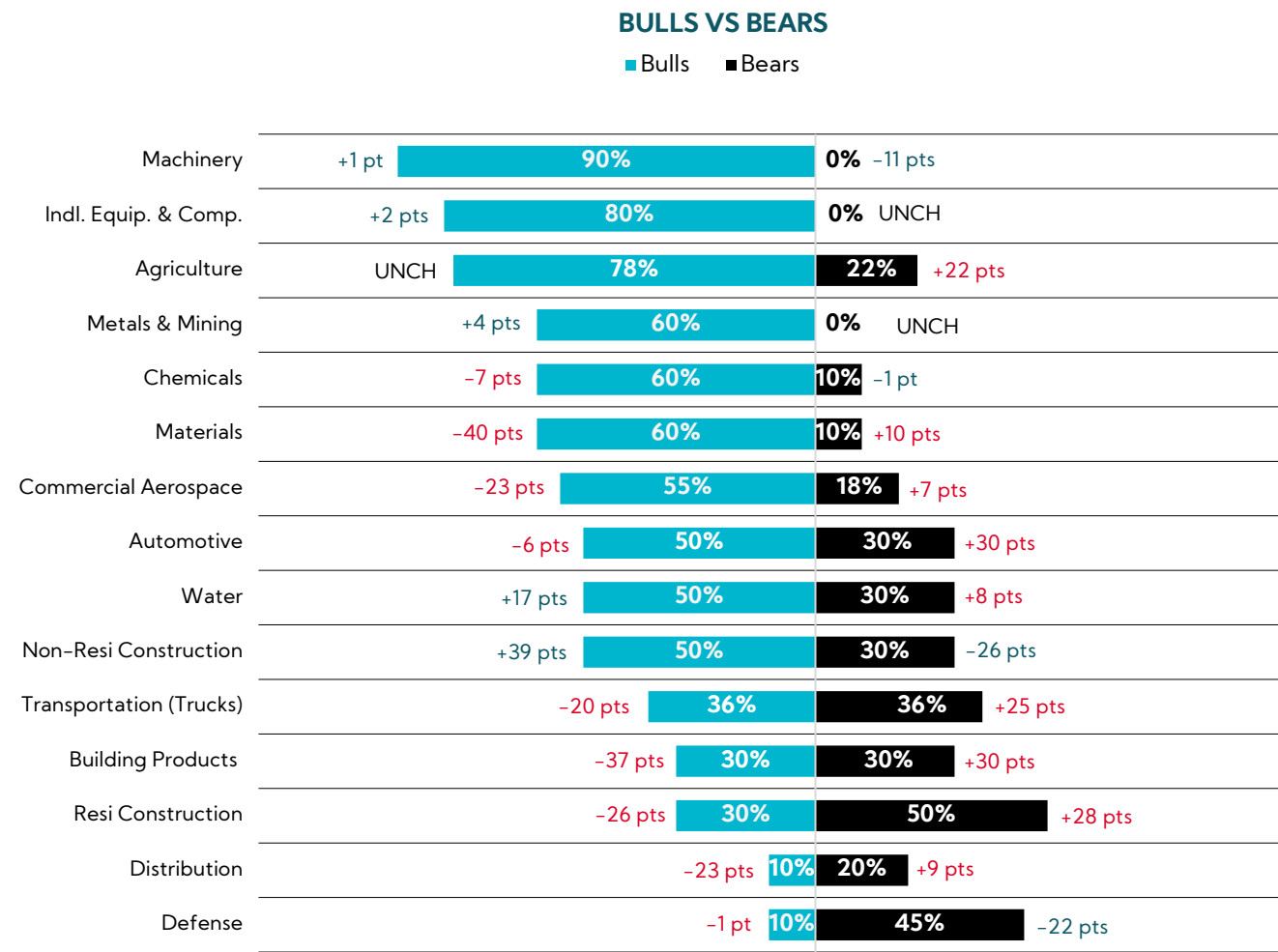
"EV/EBITDA for S&P 500 is running 25% above historical averages; publicly traded industrial EV/EBITDA is running 20%-45% above historical individual company averages and M&A multiples are running 40%-250% above historical averages for EV/EBITDA, depending on business, market, strategic fit, etc." **Sell Side, Industrials, N. America**

# Consolidation and Digitalization Most Compelling Investment Themes, While Cost-cutting Initiatives Are Also More in Focus amid Rising Inflation Concerns



# Still More Bulls than Bears amid Some Softening Optimism and Significant Industry Shifts Identified

*Non-Resi. Construction sees the most favorable shift, while Resi. Construction and Building Products see greatest pullback*



# We Are A Specialized Research and Advisory Firm

## Focused on Helping Public Companies Realize Their Value



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### TRUSTED PARTNERS

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We simplify the complex to deliver positive outcomes with agility, precision and excellence.



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Our clients trust us. We provide explicit, no-nonsense counsel with objectivity and candor.

A person in a red jacket stands in the bright, white light of a cave entrance, silhouetted against the glow. The interior of the cave is dimly lit with a deep blue light that highlights the intricate, wavy textures of the rock walls and ceiling. The floor is covered in dark, wet-looking rocks and debris.

*corbin*

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