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DOV.N - Q2 2022 Dover Corp Earnings Call

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OVERVIEW:

Co. reported 2Q22 YoverY organic revenue growth of 7%. Expects full-year 2022 adjusted EPS to be $8.45-8.65.

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PRESENTATION

Operator

Good morning, and welcome to the Dover Second Quarter 2022 Earnings Conference Call. Speaking today are Rich Tobin, President and Chief Executive Officer; Brad Cerepak, Senior Vice President and Chief Financial Officer; and Jack Dickens, Senior Director of Investor Relations. (Operator Instructions)

As a reminder, ladies and gentlemen, this conference call is being recorded. (Operator Instructions) Thank you. And I would now like to turn the call over to Mr. Jack Dickens. Please go ahead, sir.

Jack Dickens

Thank you, Emma. Good morning, everyone, and thank you for joining our call. An audio version of this call will be available on our website through August 11. The replay link of the webcast will be archived for 3 months.

Dover provides non-GAAP information. Reconciliations between GAAP and adjusted measures are included in our investor supplement and presentation materials, which are available on our website. Our comments today will include forward-looking statements based on current expectations. Actual results and events could differ from those statements due to a number of risks and uncertainties, which are discussed in our SEC filings. We assume no obligation to update our forward-looking statements.

With that, I will turn the call over to Rich.

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

Thanks, Jack. Good morning, everybody. Let's start with the performance highlights on Slide 3. Our team delivered a strong second quarter performance, which led to record quarterly revenue and sequential year-over-year earnings growth.

Consolidated organic revenue growth of 7% in the quarter as our businesses continue to capitalize on strong backlogs and pricing actions continue to take hold. We believe our ability to execute and provide needed capacity in today's challenging environment has led to noteworthy share gains in multiple markets, which is positive for our continued growth.

Component shortages and COVID lockdowns in China did negatively impact shipment volumes and, consequently, efficiency and fixed cost absorption in several businesses during the period. Despite these difficulties as well as FX headwinds, our absolute segment profit increased year-over-year and operating margin improved sequentially in the quarter, driven by cost controls, good volume and meaningfully improving price cost dynamics.

Our strong balance sheet provides flexibility for value-creating capital allocation initiatives. We are investing in capacity expansions and productivity improvements across many of our operating companies to capitalize on secular revenue growth opportunities, capture market share and drive improvements in operational performance.

The recently-announced Malema acquisition will enhance our biopharma business, closed on July 1, and we continue our pursuit of attractive bolt-on acquisitions. We also repurchased $85 million worth of shares in the second quarter, and will continue to proactively evaluate capital deployment alternatives through the remainder of the year.

Our strong backlog, constructive demand outlook and execution playbook position us well to deliver growth in revenue and earnings amidst an increasingly uncertain grow economic backdrop. We are maintaining our 2022 adjusted full year guidance of $8.45 to $8.65 per share.

I'll skip Slide 4, which shows the detailed quarterly results. Let's move on to Slide 5 to discuss segment performance. Engineered Products revenue is up 19% organically in the quarter on broad-based strength across the portfolio in major geographies as well as pricing actions. Margins were up 130 basis points sequentially, and we expect the trend to continue through the second half as price/cost spread continues to roll forward.

Clean Energy & Fueling volumes were driven by strength in clean energy components, vehicle wash and below-ground fueling components offset by the expected roll-off of EMV-related demand in North America, which peaked in the comparable quarter last year.

Margins in the quarter were down year-over-year on lower volumes and constrained input and, to a certain extent, mix. The sequential margin improvement was significant, however, at 410 basis points versus last quarter, driven by improving cost dynamics and product mix.

In Imaging & ID, our volumes in our core marketing and coating business were constrained by electronics and other import shortages as well as COVID lockdowns in China, which offset growth in our serialization of brand management software businesses, FX as a material negative headwind to absolute revenue profits in the segment given its large base of international revenue.

Q2 margins in Imaging & ID were impacted by lower volumes and production stoppages in Asia but improved sequentially. The team has done a good job in cost containment and finding alternative suppliers to alleviate supply chain constraints, and we are confident about good margin conversion in the second half.

Pumps & Process Solutions posted a 7% organic growth. We saw strong double-digit growth in our core non-COVID biopharma business as well as robust growth in medical and thermal connectors, industrial pumps, polymer processing and precision components. Operating margin in the quarter remained robust at 31% plus despite a mix shift towards industrial components.

Top line in Climate & Sustainability Technologies continue to be strong, posting 11% organic growth on solid volume in heat exchangers and beverage can making as well as pricing across all businesses. Volumes in food and retail were constrained by supply chain challenges, which negatively impact cost efficiency and will result in shipments pushing out into Q4.

Comparable and sequential margins were up in the quarter on better mix and price cost, though partially offset by production efficiencies and input shortages. As you can see, we're marching towards our mid-teens operating margin target in this segment.

I'll pass it on to Brad here.

Brad M. Cerepak - *Dover Corporation - Senior VP & CFO*

All right. Thanks, Rich. Good morning, everyone. Let's go to Slide 6. The top bridge shows our organic revenue growth of 7%, driven by increases in 3 of our 5 segments. FX was substantial at 4% or $74 million headwind to our revenue growth and also to our profitability, resulting in $0.08 negative EPS in the quarter.

We expect FX to remain a headwind for the year compared to our prior expectations, and all changes in foreign currency translations from April until today are estimated to have a full year 2022 impact of an incremental $0.10. M&A contributed $49 million to the top line in the quarter, a product of $84 million from acquisitions partially offset by $34 million from the Unified Brands divestiture.

We saw organic growth across the U.S. and Europe. Asia was flat organically in the quarter as China was down 4%, driven principally by COVID lockdowns offset by growth in other parts of the region. Our businesses in China have resumed operations and are currently seeing recovery in production in regionally-sourced components.

On the bottom of the chart, bookings were down year-over-year, primarily due to foreign exchange and a one-off $74 million debooking in beverage can making due to customer financing limitations. Likewise, our backlog was negatively impacted by the aforementioned debooking as well as a negative impact from FX.

Let's go to the earnings bridges on Slide 7. Before I get into the charts, I want to remind everyone we now exclude the impact of acquisition amortization accounting from our segment earnings, which avoids a deal-related noise quarter-to-quarter and better aligns the basis of our segment earnings presentation with our consolidated adjusted EPS. This change had no impact to our GAAP earnings or adjusted EPS.

Now to the charts. Segment earnings were up $9 million in the quarter on improved volumes and price costs, though partially offset by supply chain constraints and foreign exchange headwinds. Segment margins were down 80 basis points.

Adjusted net earnings improved by $10 million, driven by higher segment earnings and favorable corporate expenses partially offset by higher taxes. The effective tax rate, excluding discrete tax benefits, was approximately 21.5% for the quarter, comparable to the prior year period.

Discrete tax benefits were lower than the prior year at $4 million in the quarter or approximately $0.03 of EPS. This compares to discrete tax benefits of $0.08 in the second quarter of '21. We expect our back half tax rate to be in the range of 21% to 22%.

Our cash flow statement is on Slide 8. Free cash flow declined in the first half of the year, driven by working capital investments and inventory necessitated by the high backlog supply chain constraints and exacerbated by input shortages preventing completion of some work in process inventory in the quarter as well as higher receivable balances on growing sales.

The quarter also included $43 million tax payment related to the sale of Unified Brands. Capital expenditures were up year-over-year and are principally in support of our robust growth expectations across several businesses.

Free cash flow was 6% of revenue in the quarter and would have been 8% excluding the UB tax payment. We expect cash conversion to improve in the second half of the year, more in line with typical cash conversion seasonality in our businesses, driven by earnings conversion and inventory reductions.

With that, I'm going to turn it back to Rich.

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

All right. Thanks, Brad. Let's go to Slide 9. This slide is our current view of the demand outlook, operational environment and margin drivers for the remainder of '22 by segment. We expect top line in Engineered Products to remain robust based on elevated backlogs and implemented price increases.

Vehicle Services continues to see a constructive demand environment across all geographies with particular strength in North America. Demand for refuse collection vehicles and parts remains very strong, and our Connected Collections digital business is significantly outperforming expectations.

Our backlog includes fully implemented price actions that support the projected recovery in margins. We expect volume productivity and improved price cost spread to be positive drivers of earnings accretion and margin improvement in the second half of the year.

In Clean Energy & Fueling, we expect to see robust growth in the second half of the year after a roughly flat first half. We continue to see solid demand in North America for below-ground retail fueling, fuel transport, vehicle wash and software solutions.

Our acquisitions in clean energy components continue to outperform their year 1 acquisition models, and we have already begun to deploy capital in these businesses to expand capacity and improve productivity. We expect margin performance to improve in the second half on stronger volumes and mix, which will drive improved full year margins in this segment.

We expect volumes in Imaging & ID to improve as component shortages (inaudible), with China recovering from second quarter COVID shutdowns. We continue to work to identify alternative electronics providers to alleviate component bottlenecks going forward, and we're beginning to see some inquiries and improved order rates for large-scale printers and digital textile printing, a positive development in an industry that has experienced a prolonged recovery. We expect margin to improve in the second half and better volume and cost containment while keeping a close eye on FX.

In Pumps & Process Solutions activity, industrial pumps remain solid. Polymer processing has booked several big projects that lay the foundation for a very strong second half, and we recently received our single largest order ever for the business in early July.

Precision Components continues its upward trajectory in both bearings and compressor components across all geographies as investments in energy sector pick up. We expect the current below-normal demand trend in biopharma to continue for the balance of the year as biopharma manufacturers finish transitioning their R&D pipelines and production systems from COVID-related businesses to other growing biologic therapies.

We expect Climate & Sustainability Technologies to post double-digit organic growth this year, driven by large backlog and pricing initiatives. Demand remains robust across all lines in food retail. While input shortages have hampered food retail shipments, they are expected to improve, resulting in a catch-up of deferred shipments into the second half of the year. Our heat exchanger business is positioned well on strong order rates across all geographies and end markets, in particular in the European heat pump business.

In Belvac beverage packing equipment, business continues to work through its record backlog. We have already been awarded new projects in Q3 to materially offset the debooking in Q2. We expect margins to improve year-over-year on volume leverage and positive price/cost dynamics and normalizing supply chains.

Let's go to Slide 10. I presented this slide at a recent conference, but it bears repeating as not everyone attended the event and the topic continues to be actively debated. There is a view that booking rates are the sole predictor of demand and revenue growth, and negative year-over-year bookings on top of a record 2021 are somehow spelling trouble. None of us know what the future holds, especially in the current environment, let's level set on the basics here.

First, if you look at our revenue and bookings, they've historically been correlated. But because of demand wave coming out of the pandemic coupled with extended lead times from supply chain issues and some change in product mix, our bookings jumped in 2021 to $9.4 billion, well ahead of our revenue last year and our guide for '22 revenue.

That resulted in backlogs that are at record highs, roughly double where they have normally been on a 12 months revenue basis. That, over time, should come down, which is healthy because it means our lead times are coming down and global supply chains are improving.

Our backlog is sufficient to feed revenue growth for a significant period, and it's worth noting that our backlogs midway through the year are still higher than they were at the beginning of the year. And despite a decline in bookings, our book-to-bill ratio so far this year is still above 1 and in line with historical trends. Our current booking and backlog trends should position us to enter 2023 on solid footing.

Let's move to Slide 11, where we show historical first half versus second half margin performance. Historically, Dover has generated higher margins in the second half of the year. Last year was an anomaly of input inflation and supply chain constraints and COVID shutdowns hit the second half.

Our sequential margin trajectory is upward and progressing largely as expected, and we remain confident about the positive second half margin dynamics in line with historical seasonality, although I would note that Q4 will contribute more to absolute profits than normal on backlog and order timing and as we liquidate a large work in progress balances of inventory.

Make no mistake, we remain concerned with the inflation trajectory and general macro backdrop and the different demand scenarios that are possible in 2023. We have a playbook to act decisively to adapt both from a cost structure and working capital perspective to the different demand conditions. But sitting here today, looking at our backlog, significant portions of our portfolio were sold out for 2022, so we would expect the order rates to inflect positively as we go into the second half.

We have levers that are not demand dependent. We have positive contributions from our organic capital deployment and productivity initiatives, and our 4 enterprise pillar efforts will positively contribute to next year's earnings. We also have very interesting and underappreciated portions of our portfolio where secular demand growth will outperform the broader industrial market.

In closing, I'd like to thank my colleagues around the globe for their continued dedication to strong performance in a demanding operating environment. And Jack, I'll hand it back to you, and we can get to the Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) We'll take our first question from Andrew Obin with Bank of America.

Andrew Burris Obin - *BofA Securities, Research Division - MD*

Just -- you mentioned FX impact in the quarter, $0.08. What was it versus expectations? And what does the new guide assume for FX impact on EPS basis versus the previous guide?

Brad M. Cerepak - *Dover Corporation - Senior VP & CFO*

Well, okay. I'll take that. Within the quarter, the impact was about $0.02 of our -- against our expectations. I said for the full year, from here forward, it would be about $0.10.

And I think you're asking me specifically what kind of forecast rate are we using. I could say we're using a euro of about $1.05. Today, it's trading at about $1.02. So maybe the headwind is a little bit higher. But we'll see. We'll see what happens now going forward, especially with the ECB raising rates.

Andrew Burris Obin - *BofA Securities, Research Division - MD*

Got you. And just another question on commodities. Commodity is broadly down from their peak, so how should we think about -- you definitely highlighted that supply chain is getting better into the second half. But how should we think about that flowing into Dover cogs? Is it a 6-month lag? Is it a 12-month lag?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

On the commodity side, we get the majority of it in the second half, right? So all of that has been in inventory for some period of time. What we've been waiting for is the pricing to roll forward. So we've seen a significant improvement in Q2. And the expectation is on the backlog, the raw materials being fully priced in the back half of the year and those businesses that are exposed to raw materials, and that's why we're confident about the margin accretion potential.

Andrew Burris Obin - *BofA Securities, Research Division - MD*

And is there any sort of incremental margin just as effects create some incremental headwinds? Is there incremental margin of safety from commodity decline as we think about towards exiting the year?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

That's too complicated for me, Andrew. Over the last, what, couple of weeks, we've watched a significant devaluation of the euro against the dollar and we were modeling if that pace was to continue. it's pretty drastic.

So as Brad mentioned, I think there's been some recovery and some noise out of the ECB about raising interest rates, buffering that impact. But it's -- we're going to have to see. And remember, too, that we're going to convert at average rates. So you've got to be careful about taking spot rates and then trying to run the math on the second half of the year.

Brad M. Cerepak - *Dover Corporation - Senior VP & CFO*

But I would just add that as it relates to price commodities. I feel good about the fact that all of our price actions are enacted going into this back half. And so we'll see what happens with commodities. I mean that's basically all we can say is, we'll see.

Operator

Our next question comes from Jeff Sprague with Vertical Research.

Jeffrey Todd Sprague - *Vertical Research Partners, LLC - Founder & Managing Partner*

Just 2 for me. First, Rich, just on this Belvac situation. We tend to think of the customers, Coke, Pepsi, Crown, Ball, et cetera. So a little surprised to hear if somebody had a financing issue. Could you just elaborate a little bit more on what happened there? And then maybe the backfilling you're talking about is somebody stepping in and taking those slots.

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

Yes. I mean the -- look, capacity has been constrained in can making for 3 years now, right? And that's what's been driving a lot of the capital investment by the can makers. But what you've also seen is a lot of companies that rather than go into the can makers are vertically integrating.

That happened to be a particular project in Eastern Europe, which was a vertical integration play with the blow-up of the equity markets, and financing conditions changed. The order got canceled. But having said that, like I said, subsequent events, we got a $40 million order last week. So we had to debook it. That's life. None of the revenue and earnings for that particular order impact 2022. That was actually a 2023 project.

Jeffrey Todd Sprague - *Vertical Research Partners, LLC - Founder & Managing Partner*

Great. Interesting. And then just on the trajectory for the year here. I mean clearly, what you're saying about price cost and trends would indicate a sequential improvement in Q3 versus Q2, but you also are signaling a little bit more Q4 weighting. Could you just give us a little more color on how you expect the back half to play out here, just to make sure we're all properly triangulated?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

Sure. Look, I mean, at the end of the day, this was the quarter where we really had to chin the bar because that was the highest profitability quarter since the demerger or the spin-off, that we had to chin the bar. To the extent that we chin the bar considering everything was going on, this is the one we're probably most worried about this year, and we chin the bar.

So my comment on just the seasonality of the back end of the year, you can see the chart that we put into the presentation. I would just caution that because of this issue about all this work in process that we have, I would expect that to continue through Q3, meaning that we're going to actually pushing a lot more out the door in Q4 than we historically have been. As you know, generally speaking, we would kind of run flat out and then run for cash in Q4 historically.

The supply chain issues are not repairing themselves, at least sitting here today, at the speed that would allow us to deplete a significant part of our backlog and our WIP in Q3. So it's going to move into Q4, which is all baked into the full year forecast. So it was more of a comment that'll just be -- not that we give a damn about quarterly results. We're a full year company here. But I think that Q4 will be higher proportionally in terms of earnings than the historical trend.

Operator

Our next question comes from Scott Davis with Melius Research.

Scott Reed Davis - *Melius Research LLC - Founding Partner, Chairman, CEO & Research Analyst of Multi-Industry Research*

Sharp move we saw in FX. I mean is there a point where there's a demand destruction challenge? Is it -- is there -- and perhaps maybe framing how much of your product is kind of moving from dollar-based regions to non-dollar-based regions would be helpful in that regard. But is there a certain point where you start to get nervous?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

Well, I'm more nervous about the European macro than I am about FX. We don't ship hardly anything from the U.S. into Europe where we run into problems with Euro dollar of any consequence. It is a bit of a -- and I don't think that there's a significant competitive advantage that we've been taking advantage of with a lower dollar versus the Euro over time.

So I don't -- from a demand point of view, I don't think FX is an issue. I think that European macro is more of an issue. We don't see the effects of it today, but I mean, we're not naive. I mean things aren't great with energy costs where they are and everything else there.

Scott Reed Davis - *Melius Research LLC - Founding Partner, Chairman, CEO & Research Analyst of Multi-Industry Research*

And how about emerging markets where perhaps they have to buy in U.S. dollars for product?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

Again, we do a lot of for region in-region. The products that we ship into emerging markets are our most -- how do I want to put this? I mean there is no Asian competitor for Maag, for example.

So we come under some pressure from a pricing point of view. Maybe in the future if we assume that currencies -- the dollar remains strong against emerging market currencies, but right now, I think that between some of the bigger capital goods side, like the Maags and the Belvacs of the world, I think we can weather that.

Scott Reed Davis - *Melius Research LLC - Founding Partner, Chairman, CEO & Research Analyst of Multi-Industry Research*

Okay. And then just quickly last. The Printing & ID business. Any of your consumer goods customers delaying orders or talking about any slowdown in demand there?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

No, not really. I mean we just had some operational problems in Q2. I mean we are levered from a production point of view to Asia, to China specifically. So we've had some issue. We've had to shut our operations down there in Q2 for a period of time during the lockdown. And we are caught up in some of the supply chain on electronics components there that we ended the quarter with a decent improvement there.

So I would expect that at least on the printer portion of the business, we'll catch up in the second half. We do not see a deterioration on the consumable side.

Brad M. Cerepak - *Dover Corporation - Senior VP & CFO*

I would say we lost, in that segment, about 4 points of growth because of the shutdowns in China and the component supplies within that business, which catches up in the back half.

Operator

We'll go next to Joe Ritchie, Goldman Sachs.

Joseph Alfred Ritchie - *Goldman Sachs Group, Inc., Research Division - VP & Lead Multi-Industry Analyst*

Thanks. Good morning, everyone. Rich, can we start on pricing and the expectation, first, for the rest of the year? I think you guys put up 6 points of price this quarter.

And then there's a lot of discussion right now around base metal prices are deflating. How are companies -- are companies going to have to give back some pricing as commodities deflate? Can you maybe just provide some context for how that's going to work across your business?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

Yes. It's going to be an interesting dynamic. #1, price/cost inflects materially positive in the second half. All of our pricing is done for the year. So what we're -- any pricing action we're taking now is more of a '23 issue. Raw materials costs are coming down. We are not -- we didn't reprice our backlog into the headwind, and we have no intention of repricing our backlog into the tailwind, and that is something that's been an active dialogue with our customers now for -- it seems like forever, but I guess, the last year.

If prices have to come down because the raw materials are deflating, that's actually positive to margins. Because if we look at price cost on a rolling 12-month basis, you basically took a big headwind in the back half of last year into the Q1 of this year, and then you get a tailwind in the balance of the year. You end up mostly, at least on the capital goods side, a net neutral over time. It's just you have the spread between the liquidation of the backlog timing. So if it comes down in pricing, yes, it is a headwind to revenue, but it's actually a positive to operating margin.

Joseph Alfred Ritchie - *Goldman Sachs Group, Inc., Research Division - VP & Lead Multi-Industry Analyst*

And maybe just kind of following up on the piece of the business, it's not backlog sensitive to most of your business, right, the short-cycle piece? Would you expect to be just, in a deflationary backdrop, dollar neutral? Would you be dollar positive? I'm just trying to get a sense if you get to keep some of it as we kind of progress over the next 12 months.

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

Yes. On the short-cycle portion of the business, I wouldn't expect that there is not that dynamic of input cost tied to market pricing. I mean, that's really the capital goods portion of the business, both us, ourselves and our customers.

That is an ongoing dialogue just because of the proportionality of the input costs, and you can see what the dynamic is on the raw material side. On the short-cycle portion of the business, there is not that direct link. So I mean, barring the competitive environment becoming incredibly aggressive in '23. I would expect that it's our intention to keep the pricing that we've laid in.

Joseph Alfred Ritchie - *Goldman Sachs Group, Inc., Research Division - VP & Lead Multi-Industry Analyst*

Got it. No, that's helpful. If I could just squeeze one more in. Just the Pumps & Process margins finally saw some degradation this quarter. You guys have been kind of calling out mix in that business for the last couple of quarters. Is this kind of like the right new level, this like 31% type margin? Do you expect further degradation in the coming quarters?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

Yes. Look, I mean, let's not get into quarter-to-quarter performance. I think that we've been clear over the last 18 months or so that, that 30% margin is pretty much the new normal. There'll be some volatility quarter by quarter, clearly, based on mix.

And it's not all bad at the end of the day. I think on the biopharma side, the demand as our customers convert is going to be slow, as I said, in the second half of the year. We believe, in terms of our ability to retain our share of that marketplace, it's absolutely solid. We're specced in, in a significant amount of our customer base. So it's just as biopharma transitions.

And remember, too, there's other portions of that business that are dilutive to that margin. So when we post our organic growth number, I believe it was 7% more or less in DPPS for the quarter, a lot of that growth was from the industrial component side, which is dilutive to that margin. We don't try to manage segment margin. Basically, we're pushing all these companies as much as we can.

So if we have dilutive mix, that's not necessarily a bad thing. We want every piece of that segment to grow over time. And we're actually quite pleased with the performance of Maag. As I mentioned, that is its backlog is going up well into '23 now and the turnaround that we're seeing in Precision Components, which is levered to the energy sector.

Operator

We'll go next to Steve Tusa with JPMorgan.

Charles Stephen Tusa - *JPMorgan Chase & Co, Research Division - MD*

Just to be clear on kind of these price cost questions, I think Andrew was trying to ask about when you guys would see deflation given where commodity prices are today. I interpret your answer as it's not like you're seeing it in the second half. That's more of price catching up with the inflation.

So at what point would you see lower steel, lower copper run through your revenue line item? 6 months, 9 months, 12 months? Like what's the timing on that? Just to be clear on that answer.

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

Sure. I guess now we're going to go operating company by operating -- I'll give you 2 examples. I mean I think in SWEP, because that has got an inflator/deflator that probably rolls every 90 days or quarterly, you would begin to see that a little earlier. It's net neutral in SWEP in terms of its operating margin or its performance. In the other capital goods side, specifically on ESG, we wouldn't see that until mid next year, probably, based on backlogs.

Charles Stephen Tusa - *JPMorgan Chase & Co, Research Division - MD*

Right. So kind of blended for the cap goods businesses, 6 months?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

Yes.

Charles Stephen Tusa - *JPMorgan Chase & Co, Research Division - MD*

Okay. Yes. So beginning to give next year. So you're not seeing that in this year as a point and that's mostly price catching, right?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

I think it's completely manageable. I mean the -- the issue is going to be what happens to the competitive environment going into '23, and we'll see there, depending on what demand looks like.

For us, I like where we stand in terms of our competitive stacks, right? The vast majority of our business have very few global competitors, and I don't expect to see, if demand comes down, then you've got some significant headwinds in terms of the pricing environment from a competitive point of view outside of what's happening in raw materials.

Charles Stephen Tusa - *JPMorgan Chase & Co, Research Division - MD*

Got it. And then just a question on orders. Your reported orders, including that -- the backlog, the cancellation. So are you saying that those orders [next in] the third -- or just sort of run rate for the second half, that those will actually be up sequentially because of that impact of the $75 million or whatever it is? Or maybe you can just follow on sequential orders?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

What I can tell you is that the bar that we had to chin for margin and operating profit and order volume was Q2, right? So we've been guiding for a year now that this can't go on forever and orders are going to come down. But if you noticed, I'm sure you did, that our backlog didn't deplete at all.

And I think what Brad was trying to call out, you got to be really careful going forward here because FX has an impact not only on revenue and profit translation, but on balance sheets also. So -- and (inaudible) has to take care of that over time. Again, I'm not worried about our orders. I mean we've got a significant portion of our portfolio that's sold out for the year.

Charles Stephen Tusa - *JPMorgan Chase & Co, Research Division - MD*

Right. So can book-to-bill be above 1 on a reported basis for the next couple of quarters?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

Can it be? Yes.

Charles Stephen Tusa - *JPMorgan Chase & Co, Research Division - MD*

Okay. Is that in your forecast? I mean, anything can happen here.

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

To be perfectly frank, I don't -- we don't measure projected book-to-bill, right? We've got revenue forecast and earnings forecast, but no one is running around trying to count orders into the future.

Charles Stephen Tusa - *JPMorgan Chase & Co, Research Division - MD*

Except us.

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

Yes. Well, we had a discussion around here about book-to-bill orders and backlog, whether that's too much is too much. But at the end of the day, look, this notion that order rates coming down is somehow a precursor of '23 demand, I think I'd be very careful about that.

Operator

We'll go next to Andrew Kaplowitz with Citi Group.

Andrew Alec Kaplowitz - *Citigroup Inc., Research Division - MD and U.S. Industrial Sector Head*

Rich, maybe just to follow up on that. Can you give us a little more color into the puts and takes of your revenue guidance for the year? I know we just talked about currency and length, but you actually raised your organic growth guide for the year despite lowering expectations a little bit in DII and DPPS. Does your higher organic growth forecast come from more momentum in specific businesses, [DP] DCF? Or is it more confidence in supply chain easing?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

Well, let's see. #1, the back half is actually an easier comp. I've got to repeat myself again. Q2 was the comp that we had to chin and we actually grew over Q2. So if you take -- if you look at the growth that we posted for Q2, which was the highest bar that we had to chin, if you take a look at what happened in the second half of last year, right, in terms of absolute growth, we're in pretty good shape there.

Brad went through what our estimates are on FX, and we're going to be like everybody else. We're just going to have to watch that as it progresses through the year. And look, if you take a look at our cash flow, which is negatively impacted by largely inventory, we've got a significant amount of not so much finished goods, but a lot of raw materials and WIP.

And our intention is to convert a significant portion of that, which means selling it at the end of the day, again, our backlog which is -- which drives the top line, and we are going to run like crazy between now and the end of the year to liquidate that inventory position, which should be really good for the cash flow going forward.

I mean, the one watch point is going to be how much we ship in December and whether that gets hung up in receivables or not. But you know what, that's irrelevant, quite frankly. It's a timing difference. We're looking at the one that we're driving at the most is we've got to clear that WIP out of inventory, which would have the knock-on effect of clearing the raw material position that we have.

Andrew Alec Kaplowitz - *Citigroup Inc., Research Division - MD and U.S. Industrial Sector Head*

And then, Rich or Brad, maybe I can follow up on the cash flow. Obviously, you had your initial cash flow guide out there, 13% to 15% of sales. I know cash flow improved sequentially. But as you were just talking about, Rich, it seems pretty back-end loaded. Any update on sort of that original guidance or how to think about cash flow conversion over the next couple of quarters?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

Look it's -- Andy, it's basically what I said, right? There's nothing changed here about the cash flow dynamic. Our earnings are going up for the year. That's a positive. We have brought in more inventory because of all these supply chain issues. I'm not worried about it because our inventory position proportionately against the backlog that we have is fine.

We're going to flush a significant portion of the inventory in the second half of the year. What happens in payables and receivables based on timing and everything else, I think the only watch point would be on the receivables balance at the end of the year, but then the world doesn't end on January 31.

I'm not calling out that we've got an issue with the guidance and we're going to drive towards making it, but look, I think from a cash flow point of view, we're in no different position than we've been in the past and our earnings are higher.

Operator

Our next question comes from Josh Pokrzywinski, Morgan Stanley.

Joshua Charles Pokrzywinski - *Morgan Stanley, Research Division - Equity Analyst*

Rich, you mentioned, and I apologize, I jumped on the call a couple of minutes late, you've watching Europe maybe a little bit more closely than kind of worrying about macro at large. Anything in terms of progression through the quarter order rates, mix of business?

I know there's a couple of particularly economically-sensitive businesses there. I would think the retail fueling, when -- your $8 a gallon gas maybe isn't feeling awesome. But anything there that you guys -- you feel the need to point out?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

No, nothing. It was just a comment on a watch item where I think the question was more, are we more worried about FX? FX is what it is at the end of the day. I don't think it changes the dynamic where we think it's a headwind of our ability to compete in the Euro zone because of some -- that we're shipping dollarized products into Europe. We don't.

Clearly, Europe, from a macro point of view, is a watch item. We're not naive here. We don't see it yet, but we're paying very close attention to it. And then we run a variety of scenarios depending on what we think could happen to demand, what we do to our cost structure. And that was the comments I made in the presentation of we've got a playbook here that says when things start moving, how quickly we can move, and we believe that we can move faster than the macro (inaudible).

Joshua Charles Pokrzywinski - *Morgan Stanley, Research Division - Equity Analyst*

Got it. That's helpful. And then I guess maybe coming out a little bit more strategically. You've been talking about near-shoring or kind of broader supply chain investment by the industrial world for a while now. At the same time, you're seeing some of that, I guess, start to improve.

Anything that you think with improvement people sort of forget about or move on from? How are you guys thinking about this transition maybe from like triage mode to how you want to address some of these supply chain issues on a longer-term basis?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

Yes. Look, I mean we've been the recipient, unfortunately, in the first half of the year of our own suppliers going through that transition, which has led to some of the headwinds that we've seen. So I think from a longer-term perspective, it's healthy.

So you see quite a bit of capital investment going in -- let's call, into NAFTA for lack of a better word, but that's -- these are industrial products, and they're not easy to move around, and we're all kind of going through that transition. Interestingly, from a CapEx point of view, our CapEx-related businesses are very strong.

So the order rates that we're seeing in Belvac and Maag and what's going on in Precision Components and what's going on in Refrigeration, those are all, let's call them, CapEx-related businesses. And from a backlog perspective and a demand perspective, I mean, they're all sold out for the balance of the year, and we're actually booking into '23.

So I know there's a big debate going on out there between consumer recession versus industrial recession. The CapEx sitting here today, I think that we're more positive than negative in terms of CapEx demand or CapEx-related demand going into '23.

Operator

Our next question comes from Deane Dray with RBC Capital Markets.

Deane Michael Dray - *RBC Capital Markets, Research Division - MD of Multi-Industry & Electrical Equipment & Analyst*

Maybe we'll just stay on that same CapEx theme. Any change in your thoughts regarding CapEx spending expectations for the year for you guys?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

On our own? No. No. I think that what we have modeled in for ourselves through the year is we're all done. So I mean I don't think we could -- we can't spend what we've got in the plan now. So no, I don't think -- barring a customer showing up and saying, "I want X," which clearly we would invest behind right now, I think that we're done in terms of commitments, and you'll see it reflected in the cash flow as we go through the balance of the year.

Deane Michael Dray - *RBC Capital Markets, Research Division - MD of Multi-Industry & Electrical Equipment & Analyst*

Got it. And in reference to the early discussion about counting orders, can you talk a bit more about that single largest order? You said it was in Pumps & Process, what the application is. How competitive and how might the margins shake out versus the segment normalized average?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

It's polymer processing where the order came from. It's in Asia and it's slightly dilutive to the consolidated margin but still very good margin.

Deane Michael Dray - *RBC Capital Markets, Research Division - MD of Multi-Industry & Electrical Equipment & Analyst*

Got it. And how competitive was that?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

It's -- they're all competitive. Having said that, it's better to be competing with -- against 2 other people versus 10 people. And by and large, the vast majority of the portfolio is competing against 2 or 3 people. So it's competitive, but not crazy.

Deane Michael Dray - *RBC Capital Markets, Research Division - MD of Multi-Industry & Electrical Equipment & Analyst*

That's helpful. And just last one, if I could. Last quarter, when we talked about pricing, Rich, you said you might be pricing more along the lines of surcharges. How has that played out?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

You know what, I don't -- I think that because of the dynamics of raw materials, we haven't had to do surcharges since then. I think it was an option that we were -- we are basically -- I think that when we had the discussion last time, as we've done a significant a lot of pricing here, that's all modeled in the roll forward for the balance of the year. So kind of like our pricing was done, assuming what we have in our EPS forecast.

And that -- I think the response to the question is, well, what if we see input costs go up again, what are you going to do? And the answer was, at this juncture, we'd probably take a look at doing surcharging. We've done some but very little because of the fact that we haven't seen a degradation, we actually -- it's more of a tailwind going forward input cost than it's been a headwind over the past year.

Operator

Our next question comes from Brett Linzey with Mizuho.

Brett Logan Linzey - *Mizuho Securities USA LLC, Research Division - Executive Director*

I wanted to come back to capital deployment. You made a comment about proactively evaluating other various alternatives. Could you just put a finer point on that? Is it buybacks, special dividend? What's all under consideration? And then if it is the buyback, would you consider levering up? Or was this just a balance between bolt-on buyback and free cash flow?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

I think that the capital markets would have to get pretty grim before we levered up to do it. So it's more on deployable cash flow, meaning that if we were -- if our pipeline, from an inorganic point of view, was low, that we would not sit on our projected cash flow balances for a prolonged period of time.

And so then we have optionality for capital return to shareholders. Our bias there is share repurchase over doing a special dividend as we sit here today. But that's always a discussion with the Board of Directors.

Brett Logan Linzey - *Mizuho Securities USA LLC, Research Division - Executive Director*

Okay. Great. And then just shifting to the European pump business there. How large is that on a run rate basis currently? And I know the order rates have been pretty good there, but can you just speak to the scope of further opportunity in that business? And then specifically, how Dover is competitively positioned for the opportunity?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

Yes, we don't really get into giving out revenues by segment because that's a slippery slope that -- these conference calls will last 1,000 years. It's a good -- it's material to the full year revenue. I think the reason that we called it out was the scale of the particular purchase order as a proxy for kind of CapEx demand going forward.

So it's a good order proportional to the revenue. That business is sold out for the year. So it's all '23 that we're booking for now. So it's a precursor for the solidity of that particular business' revenue stream going into '23.

Operator

Our final question comes from Nigel Coe with Wolfe Research.

Nigel Edward Coe - *Wolfe Research, LLC - MD & Senior Research Analyst*

Just I thought it would be useful to go back to the guide, maybe Brad, this is for you. So $0.10 from FX headwinds at current plan rates. It sounds like that's offset by a point better organic growth. Is there anything else in the plan that's moving around? Seems like tax is coming in a bit better. But anything on corporate, et cetera, that we should bear in mind?

Brad M. Cerepak - *Dover Corporation - Senior VP & CFO*

No, I don't think so. I think corporate was a little bit favorable in the quarter for reasons of booking accrual rates and things of that nature, but corporate kind of gets back to a normal pace in the back half of the year. As I said, the headwinds is $0.10 versus our last expectation. That's built into our guide, same as it is on the revenue side.

So revenue and earnings are reflective of what we said was our current thinking about FX rates. The organic increase, another way to think about that is we chin the bar in Q2. We had a good Q2. We see that helps us for the full year as well and solidifying price is also helpful. So there's no huge movements there. It's more refinement than anything else.

Nigel Edward Coe - *Wolfe Research, LLC - MD & Senior Research Analyst*

Okay. Great. That's great. And then, Rich, maybe for you, a bit more expansive question on Europe for me. The sort of the top-down view on Europe is dismal. The micro sort of company data is actually coming in a lot better. It's a little bit surprising.

So just wondering what you're seeing on the ground in Europe. And I'm just wondering how concerned are you by the prospect of gas rationing, energy inflation? And are you seeing anything sort of unusual in terms of behavior from customers in Europe right now?

Richard Joseph Tobin - *Dover Corporation - President, CEO & Director*

Nothing unusual. I mean we -- Europe is probably more levered for export than NAFTA is for us. So it's not -- the proportionality of Europe for Europe is actually lower than it is for NAFTA, which proportionately is very high, so there is a bit of a buffer there. So I mentioned before, with Maag having its single biggest order, the European company that's shipping into Greater Asia, and that business remains strong.

Look, it's hard to tell right now. We don't see a lot of negative -- negativity. We don't see any cancellations in orders that we have in backlog in Europe right now. It was just more of a -- when we talk to our customers and we talk to our employees, this isn't good and what's going to happen here. But right now, we don't see anything where things are rolling over.

But clearly, we are running scenarios, a variety of them. If Europe was to run into in some problems, what are we going to do? And like I mentioned before, I think that we've got a playbook that allows us to protect operating margins under a variety of demand scenarios.

And I think we proved that in 2020. We would just run that same playbook back again. But I mean I wish I could be more specific. Right now, everybody is concerned on what's going on in the macro in Europe, but we don't see it rolling to a situation where it's overtly negative yet.

Operator

That concludes our question-and-answer period in Dover's Second Quarter 2022 Earnings Conference Call. You may now disconnect your lines, and have a wonderful day.
