07-May-2025

Flex Ltd. (FLEX)

Q4 2025 Earnings Call

CORPORATE PARTICIPANTS

David A. Rubin
Vice President-Investor Relations, Flex Ltd.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

Kevin S. Krumm
Chief Financial Officer, Flex Ltd.

OTHER PARTICIPANTS

Samik Chatterjee
Analyst, JPMorgan Securities LLC

Steven B. Fox
Analyst, Fox Advisors LLC

Ruplu Bhattacharya
Analyst, Bank of America

George Wang
Analyst, Barclays Capital, Inc.

Mark Delaney
Analyst, Goldman Sachs & Co. LLC

Christian Zyla
Analyst, KeyBanc Capital Markets, Inc.

MANAGEMENT DISCUSSION SECTION

Operator: Thank you for standing by. Welcome to Flex's Fourth Quarter and Fiscal Year 2025 Earnings Conference Call. Presently, all participants are in a listen-only mode. After the speakers' remarks, there will be a question-and-answer session. [Operator Instructions] As a reminder, this call is being recorded.

I will now turn the call over to Mr. David Rubin. You may begin.

David A. Rubin
Vice President-Investor Relations, Flex Ltd.

Thank you, Melissa. Good morning, and welcome to Flex's fourth quarter and fiscal 2025 earnings conference call. With me today is our Chief Executive Officer, Revathi Advaithi, and Chief Financial Officer, Kevin Krumm, who will give brief remarks followed by Q&A. Slides for today's call as well as a copy of the earnings press release and summary financials are available on the Investor Relations sections of flex.com. This call is being recorded and will be available for replay on our corporate website.

As a reminder, today's call contains forward-looking statements which are based on our current expectations and assumptions. These statements involve risks and uncertainties that could cause actual results to differ materially. For a full discussion of these risks and uncertainties, please see the cautionary statements in our presentation, press release, or in the Risk Factors section on our most recent filings with the SEC. Note this information is subject to change and we undertake no obligation to update these forward-looking statements.

Please note, unless otherwise stated, all results provided will be non-GAAP measures and all growth metrics will be on a year-over-year basis. For the full non-GAAP to GAAP reconciliations can be found on the appendix slides of today's presentation as well as in the summary financials posted in the Investor Relations website.

Now, I'd like to turn the call over to our CEO. Revathi?

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

Thank you, David. Good morning and thank you for joining us today. Starting with our fiscal Q4 results on slide 4, we had a very strong finish to the year. Revenue came in at $6.4 billion, growing almost 4% year-over-year. Adjusted operating margin came in at 6.2%, which is another quarterly record and the second quarter in a row with adjusted operating margin above 6%. We delivered adjusted EPS of $0.73, up 28% over last year.

Now, looking at the full year results, we achieved another year of record annual adjusted operating margins coming in at 5.7% despite continued macroeconomic headwinds. And this is our fifth consecutive year of double-digit adjusted EPS growth, reaching a record level of $2.65 per share. Also, we generated over $1 billion in free cash flow, another record high. And for the second consecutive year, we exceeded our 80-plus percent adjusted free cash flow conversion target.

This year, we drove strong growth in key markets such as the data center as we continue to shift the portfolio towards more profitable business. We executed on multiple program fronts, completed several key acquisitions, and we won two PACE Awards in the automotive space with our NVIDIA Drive AGX-powered Jupiter Compute platform and our Backup DC/DC Converter.

Throughout all of this, we maintained our relentless focus on operational efficiency. Another year of strong results once again demonstrates our ability to effectively navigate a challengingly macroeconomic environment and deliver value to our shareholders. These achievements also speak to the extraordinary dedication of our team who delivered these results under challenging market conditions. This has been the theme for the last several years, and it's important to understand how we got here.

Now turning to the next slide. From the beginning, I have emphasized our focus on winning the right kind of growth that would ultimately transform this company. Since 2020, we have executed our Flex Forward strategy. We've made aggressive portfolio management decisions that positioned us to shift towards higher value businesses. And by integrating thoughtful organizational changes and operational innovations, we have built a more efficient and resilient company.

From this transformational strategy, we've delivered multiple years of consecutive record level adjusted operating margins and earnings per share. This performance validates our strategic direction and shows our ability to create sustainable value through the cycle.

As you will recall, on our Investor Day last May, we formally unveiled the next phase in our evolution, our EMS + Products + Services strategy. This approach builds on our world-class advanced manufacturing and supply chain capabilities, adding proprietary products and expanded value-added services that provide greater vertical integration and customization at scale.

Our power products further differentiates Flex as the only provider with a comprehensive portfolio spanning the data center from grid to chip. We believe that this evolved strategy will generate greater value for our customers, more integrated engagements and, of course, margin accretive growth opportunities.

Now turning to the next slide. Our data center business exemplifies this strategy in action. Total data center revenue grew about 50% year-over-year in both Q4 and for the full year, and reached approximately $4.8 billion in fiscal 2025 at accretive margins. We also strengthened our competitive position through several acquisitions aimed at solving critical challenges around power, heat and scale.

Our data center revenue is comprised of two parts, cloud and power. In FY 2025, our cloud programs generated about $3.5 billion as we provide end-to-end customized hyperscale rack solutions. Cloud operations are increasingly seeking more complete solutions to improve efficiency and cost at the scale they require. This year, we further enhanced our solution with direct-to-chip liquid cooling capabilities through our JetCool acquisition.

Our power products, which is a combination of our embedded and critical power solutions, generated about $1.3 billion in revenue in fiscal 2025. As you can see in the graphic, embedded power solution starts at the board level with our power modules managing power to the GPU or custom ASIC all the way through the rack.

Critical power solutions, is the other part of our power portfolio, which covers everything above the rack and through data center facilities, including our power pods that provide a fully customized modular data center power-in-a-box, which is critical in supporting faster time-to-market and future flexibility as data centers evolve.

Through our Crown Technical acquisition, we enhanced our critical power capabilities in the data center and expanded our addressable market into grid modernization. As you can see, we've truly differentiated ourselves as the only company providing both end-to-end IT cloud integration and an innovative power portfolio that spans from grid-to-chip. This synergistic combination reinforces our position in the evolving AI data center ecosystem, given the convergence between compute and power. Our value proposition is evident in the strength of our data center revenue growth at accretive margins.

As we look to next year, we expect data center revenue to grow around the mid 30% level with power likely a little above that rate as we ramp domestic capacity, and cloud to be slightly below due to difficult comps.

Now turning to slide 7. Regarding tariffs, here are few things to keep in mind as we navigate the evolving situation. As we previously stated, tariffs are a pass-through cost. Mexico is our largest revenue center, and over 90% of what we produce there is USMCA compliant. Very little of the product manufactured in China comes to the US. However, we do procure raw materials from China and other countries that may still be impacted by higher tariff, so this does add costs that we will ultimately pass through.

As a trusted global manufacturing partner with deep supply chain expertise, we have become the first call for customers to help navigate today's complex trade and tariff environment. Through our proprietary pulse simulation platform and our team of supply chain experts, we have visibility in potential tariff impact by customer and by country, and are currently working with many customers to develop durable tariff mitigation strategies. This approach builds on our success, guiding customers through Tariff 1.0 and other recent major geopolitical events.

What's particularly noteworthy is how quickly the situation has progressed from conversations about potential location scenarios to customers moving forward with transition plans for North American manufacturing capacity. We believe these moves are reflective of a longer-term trend towards regionalization, as well as the value of our footprint and the trust customers place in our execution. We were early in establishing the right footprint capabilities and labor pools in key markets. Our actions and strategic investments have enabled us to have the right ecosystem in place today.

Flex's global operational footprint now covers over 48 million square feet. Last year, we expanded four new strategic locations, predominantly in the US, which now encompasses 7 million square feet across 17 facilities and further expandability.

When combined with our 9 million square feet in Mexico, we now command one of the largest advanced manufacturing footprints in North America. This expansion has been tied to current customer demand, especially with cloud and power programs. We'll continue to be selective on new programs in North America as we prioritize capacity for initiatives that deliver maximum value and align with our longer-term strategy.

Additionally, our EMEA footprint now exceeds 11 million square feet, also maintaining our position as one of the region's largest diversified manufacturing providers. You can see how our extensive footprint and operational agility have now become tremendous strategic assets.

Of course, there are still risks in the current tariff environment, particularly to demand and a potential slowdown in the broader economy. Still, we believe that we are well-positioned to support customers and expect Flex to remain both a facilitator and beneficiary of regionalization in the coming years.

Kevin will provide our full guidance in just a moment, but I want to make a few comments as we look ahead to fiscal 2026. Once again, this year is off to a dynamic start. As I've said before, resiliency and adaptability are embedded in our core, enabling us to navigate years of disruptions while still executing our longer-term growth and margin expansion strategy. The strength of this foundation becomes evident when you consider that despite current market uncertainty, our fiscal 2026 guidance indicates we expect to achieve 6% adjusted operating margin, reaching our fiscal 2027 target of full year ahead of schedule.

Stepping back, I remain deeply confident in our strategy and distinctive value proposition. I believe our current capabilities and competitive advantage present the strongest opportunity in our company's history. And I'm very excited about our future and the exceptional value will continue to deliver to our stakeholders.

Lastly, I want to thank the Flex team again for your continued dedication and hard work. I also want to thank our customers for their trust and partnership.

And with that, I'll turn it over to Kevin. Kevin?

Kevin S. Krumm

Chief Financial Officer, Flex Ltd.

Thank you, Revathi, and good morning, everyone. Starting with our Q4 results on slide 9, fourth quarter revenue came in at $6.4 billion, up nearly 4% versus prior year. Gross profit totaled $602 million and gross margin improved to a record level 9.4%, up 80 basis points. Operating profit was $396 million with operating margins at 6.2%, up 80 basis points. And as Revathi mentioned, this was a new record for Flex. Finally, earnings per share for the quarter increased 28% year-over-year to $0.73 per share.

Turning to our quarterly segment results on the next slide. In Reliability, revenue was $2.9 billion, down 1.3%, largely driven by strength in power, offset by continued softness in core industrial and renewables. Operating income was $180 million, with segment operating margin up 40 basis points, finishing at 6.2%.

Agility revenue totaled $3.5 billion, growing a very strong 8.2%, driven by cloud demand and networking share gains, offsetting weak enterprise IT and consumer end markets. Operating income was $230 million, with operating margins up 100 basis points, improving to a new quarterly record of 6.6% on continued mix improvements.

Looking at our full year FY 2025 results on slide 11, revenue was $28.5 billion (sic) [$25.8 billion], down 2%, driven by strength in cloud and power, primarily offset by continued softness in core industrials and renewables. Gross profit totaled $2.3 billion and gross margin improved to 8.8%, up 100 basis points driven by strong mix. Operating income totaled $1.5 billion, up 15%, leading to a 5.7% operating margin, up 90 basis points, driven by favorable mix impacts and operational efficiency.

I'll point out, we hit record levels for both annual gross and operating margins this year. For the full year, Flex achieved EPS of $2.65, up 23%, driven by record operating profit and strong free cash flow conversion which contributed to another year of strong share buybacks.

Moving to our cash flow on slide 12. Free cash flow in the quarter was $325 million and for the full fiscal year, we delivered a record $1.1 billion in free cash flow. The strong performance is coming from CapEx discipline and continued focus on working capital management with outsized reductions in inventory.

In Q4, net inventory was down 4% sequentially and 18% year-on-year. Inventory net of working capital advances was 56 days, a reduction of 14 days versus the prior year. For the quarter, net CapEx totaled $108 million, bringing full-year CapEx to $423 million or approximately 1.6% of revenue. In the fourth quarter, we repurchased about $300 million of stock or approximately 8 million shares.

Our capital allocation priorities remain intact. We are focused on maintaining our investment grade balance sheet, funding CapEx to support organic growth, deploying capital towards accretive M&A, and returning capital to our shareholders opportunistically through our share repurchase program. This was evident in FY 2025 as we deployed CapEx judiciously, spent about $400 million on strategic accretive M&A, and repurchased nearly $1.3 billion of stock, representing about 9% of our outstanding shares.

Turning to our segment results for FY 2025 on slide 13. FY 2025 was a highly dynamic year. Still, we delivered exceptional performance in key end markets such as data center, as well as achieving growth in medical devices and automotive power electronics, where we continue to benefit from content gains.

Macro-driven headwinds affected several end markets, including core industrial, renewables, and medical equipment. We believe these headwinds are temporary and expect these end markets to support growth in the future. Our diversified end market strategy has enhanced our resilience through market cycles, while simultaneously driving growth in our strategic focus areas.

Additionally, active portfolio management to improve mix, growth in our products business, and expanding value-added services has helped drive strong margin expansion through the cycles and in both segments.

Finally, our focus on operational excellence and efficiency is contributing to record level operating margins. In our Reliability segment, revenue was $11.7 billion, with operating margin finishing at 5.8%. Again, that's a record level for the segment. And despite the top line pressure, the team still delivered 50 basis points of margin improvement.

In our Agility segment, revenue totaled $14.1 billion, delivering a 6.1% operating margin, also a record. I'm reminded, Agility margins used to be around 2%, so that's quite a transformation and it reflects purposeful mix shift towards higher value business in all three business units.

Looking at our full-year 2026 guidance on slide 14. With respect to the current macro environment, we're taking a conservative approach to our initial guidance. We believe it's prudent to provide a wider than usual revenue range, recognizing there are a lot of variables that create uncertainty for our customers. That said, we have not expanded the range for operating margin or operating profit as we are confident in our ability to navigate this environment from a profitability standpoint, as we've done over the last few years and in other challenging situations. Additionally, we have not incorporated direct tariff impacts to our expected costs or revenues, given the rapidly changing nature of the situation. I'll explain that in further detail in a moment.

Another factor to consider as we look to FY 2026 revenue guidance, we are seeing an increasing number of customers moving to our customer-sourced inventory models, particularly in our cloud business. Financial reporting requires that the value of the customer-sourced inventory under these contracts be excluded from revenue. The net effect is that this shift in contract mix is muting our reported growth rate by excluding this activity, which is growing significantly year-on-year from revenue.

With the strong growth in our data center business, cloud is becoming a more material contributor and within cloud, we are seeing an increase in adoption of these models. In FY 2025, this customer-sourced inventory activity increased $1.5 billion and represented approximately 17% of revenue. This is versus approximately 11% of revenue in FY 2024, and is expected to increase an additional $1 billion plus in FY 2025 and 2026, which would represent approximately 20% of revenue.

We've said in the past we support our customers in either standard purchase and resell models or these consignment-like models, because they both drive operating profit dollar growth, which you saw increase 15% year-on-year in FY 2025.

The simple takeaway is that we are winning new higher value data center business, not fully reflected in growth rates, which is driving growth in operating profit and EPS and generating greater value for our shareholders.

As we look ahead, our FY 2026 expectations are revenue to be between $25 billion and $26.8 billion, adjusted operating margin to be between 6% and 6.1%. As we said in the past, as global tax rates increase we expect some headwinds. So for FY 2026, we expect our adjusted tax rate to land at about 21%. We expect adjusted EPS to be between $2.81 to $3.01 per share and we expect to generate strong free cash flow and maintain our 80% plus free cash flow conversion target.

As Revathi said, our adjusted operating margin guidance implies that we hit our FY 2027 target of 6% plus operating margins a year earlier than expected.

With regards to tariffs, it is a highly dynamic situation, but a few things to keep in mind. We expect tariffs to be a pass through cost, and we typically have strong contractual protections to allow for this. Tariffs can affect cash flow timing if there is a lag between when we pay the tariff at the border and receive the recoveries from customers. Depending on the magnitude, tariff recoveries could have an impact similar to inflation recoveries during the supply chain crisis, where we saw a slight increase in revenue growth and slight pressure on operating margins as recoveries came in as low calorie revenue.

Lastly, some Flex-owned power products could be subject to tariffs due to current material and component sourcing. While we don't anticipate this to be a material issue, we do have pricing actions underway to offset these impacts where needed.

Obviously, this is all still rapidly evolving, which is why we've excluded these direct tariff factors from our guidance. I just want to reiterate, we have a strong footprint and the right geographies, which we are confident will allow us to help our customers navigate this environment and position Flex well to benefit from the longer-term trends in regionalization.

Moving on to our initial FY 2026 segment outlook. For Reliability Solutions, we expect revenue to be flat at the midpoint, with continued strength in data center power, offsetting macro-related softness in automotive, core industrial, and renewables. For Agility Solutions, we expect revenue to be flat to slightly up, driven by sustained strength in cloud demand, networking share gains, and lifestyle wins, tempered by soft enterprise IT, telco, and consumer devices.

Finishing off with our guidance for the first quarter on slide 16. We expect Reliability Solutions to be flat to down high-single digits, largely due to expected auto weakness on tariff-related disruptions affecting customer volumes. We expect Agility Solutions revenue to be down low-single to up mid-single digits based on strong cloud, balanced against softer enterprise IT and consumer-related end markets.

For total Flex, we expect revenue in the range of $6 billion to $6.5 billion, with adjusted operating income between $330 million and $370 million. Interest and other expense is estimated to be around $50 million, and the adjusted tax rate to be around 21%. Lastly, we anticipate adjusted EPS to be between $0.58 and $0.66 per share based on approximately 385 million weighted average shares outstanding.

With that, I will now turn the call back over to the operator to begin Q&A.

QUESTION AND ANSWER SECTION

Operator: Thank you. We'll now begin the question-and-answer portion of today's call. [Operator Instructions] Our first question comes from the line of Samik Chatterjee with JPMorgan. Please proceed with your question.

Samik Chatterjee
Analyst, JPMorgan Securities LLC
Q

Hi. Thank you. Good morning, and thank you for taking my questions, and congratulations on the strong margin guide here. Maybe if I can start off with that. As we look at the margin guide for fiscal 2026, which is for 6% – a bit more than 6%, how should we think about the drivers relative to fiscal 2025 outside of maybe mix on the cloud business as that grows rapidly? Outside of mix on increasing contribution from cloud, what are the other drivers you're sort of penciling in there in relation to the strong margin guide for fiscal 2026? And I have a follow-up.

Kevin S. Krumm
Chief Financial Officer, Flex Ltd.
A

Hi, Samik. This is Kevin. I'll start on that. Yeah, you nailed it. A big driver of the mix year-on-year is going to be our continued growth in the cloud. Also data center product business, as we are in our power business, we should continue to see favorable mix impacts from that as well. I will point out, our service business, we expect continued growth there year-on-year, which should have some favorable mix impacts.

And then lastly what I'll say is, the drivers of mix that you've seen benefit our business in FY 2025 we expect to continue in FY 2026, which is in each one of our segments we expect them to continue to drive mix improvement in those segments through operational efficiency and continued productivity and leverage.

Samik Chatterjee
Analyst, JPMorgan Securities LLC
Q

Okay. Got it. And for my follow-up, given the – I think you referenced this in your prepared remarks as well, that customers are now looking for capacity, which you have in Mexico, as well as in US. Can you just give us a bit of sort of the lay of the land, what are you hearing from customers in relation to demand for either US footprint and Mexico? How much sort of capacity, flexible capacity do you have on that front? And does that present a dollar margin opportunity as well in relation to picking some high-margin business or as you go through fiscal 2026? Thank you.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

Yeah, Samik, I'd say first is definitely, for our teams, the phones are ringing off the hook as customers are trying to figure out, one is what's the impact of tariffs, and then longer term what this means to their footprint. The good part is that we've worked through this in the whole Tariff 1.0 scenario, and we've been – done a lot of work already in terms of moving footprint around for our customers over the last kind of five years. So it's not new to us.

The good news for us is that our footprint is so strong in Europe and in North America, that we have some available capacity, and where we have also announced new capacity expansions over the last year, as you have seen and heard from us, in these regions that we're able to really be thoughtful about what is the right kind of mix we want as we look at these capacity expansions. But at the end of the day, we want to help our customers, right, and that is our big focus.

So, a lot of conversations with customers on open capacity, increasing utilizations in terms of our existing equipment to drive productivity, so we can drive more volume for them from these factories. All of those things are continuing conversations. And we expect the continued shift that has happened in our footprint, that has happened in our PPE, and then as the result, continued improved margin as a result of these changes.

So, you know, while tariffs create a lot of noise and are not helpful in many ways, the changes that are happening to regionalization and to customer locations as a result of this, are really, really important to us.

And only the last thing I'd say in closing is, as customers look at things from a longer-term perspective and the regionalization will continue, we will need open capacity in North America, could be Mexico or the US, and I believe we are very well-equipped to deal with that and support them through that transition.

Samik Chatterjee
Analyst, JPMorgan Securities LLC

Q

Got it. All right. Thank you. Thanks for all the color.

Operator: Thank you. Our next question comes from the line of Steven Fox with Fox Advisors. Please proceed with your question.

Steven B. Fox
Analyst, Fox Advisors LLC

Q

Hi. Good morning and thanks for taking my questions. I had two. First off, Revathi, I was curious if you could expand on your comments you highlighted around data centers, your scale advantages. How does that play out in the new fiscal year? What are you seeing in the marketplace that is sort of playing into those advantages?

And then, Kevin, just from an inventory standpoint. Obviously, a lot of improvement there. How do we think about sort of inventories and working capital impacting the cash flows in fiscal 2026? Thanks.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.
A

Okay, Steven, I'll start off. I'd say in data centers, as I think about our overall kind of footprint and capability, right, is one is in the IT integration side that comes under our CEC business. First is having the ability to have a fully vertically integrated capability, that is where you're cutting the sheet metal, putting all the equipment together with server storage, switching devices, having the power available to do it, then also today having liquid cooling capability to scale these customer orders up, are all important.

And so, we have the ability, not only have the footprint, but have the power availability for these IT integration and the equipment and the utilization capability for rack integration, I would say unlike almost any other competitors in this region, in this area. So, scale is really, really important in the IT integration side.

On the power side, the engineering and design capability in terms of not only designing what is happening today, which is we're talking about kind of 100-kilowatt power in Iraq or higher in some cases. Being able to design that with kind of the silicon providers is really significantly important. So there, the scale of engineering capability in designing that and deploying that I think is very important for us. So on the power side, the scale comes not only from footprint but from the engineering scale and the depth of experience that exists there.

And then, the thing I said in my prepared remarks that I have said a few times before is, what is coming together is compute and power. And there is really no supplier who can put the two together other than Flex, right? And so that is a very unique capability we have that totally differentiates us. And more and more customers are asking for that today, not only in terms of the programs they're working on today, but what they're designing for the future. And that's a very unique differentiation that we have.

Kevin, I'll turn it over to you for the inventory question.

Kevin S. Krumm
Chief Financial Officer, Flex Ltd.
A

Hi, Steven. Thanks for the question. On inventory, as you asked on FY 2026, I'll point to sort of inventory trends over the last couple of years. As you know, coming out of COVID, we invested heavily in inventory and we've been harvesting that investment over the last couple of years and certainly did so again in FY 2025, which was a big driver in our record level free cash flow, which was about $1.1 billion.

As we end the year, our team has done a great job and we see inventories really ending FY 2025 at more normal levels. All that said, we do expect some improvement in our inventory rate and in our working capital rate in FY 2026, but not at the levels we've seen over the last couple of years. And that's really what's informing our 80% plus free cash flow conversion target.

The other thing I'll point out with respect to FY 2025 as we move into our FY 2026, is in our FY 2025, CapEx as a percent of revenue was about 1.6%. That's a little below our target rate, historical target rate of about 2%. So, as we go into our FY 2026, I expect our CapEx as a percent of revenue to normalize closer to that historical rate. Again, that's a contributor to our full year guide of 80% plus free cash flow conversion.

Steven B. Fox
Analyst, Fox Advisors LLC
Q

Great. Thank you very much.

Kevin S. Krumm
Chief Financial Officer, Flex Ltd.
A

Thank you.

Operator: Thank you. Our next question comes from the line of Ruplu Bhattacharya with Bank of America. Please proceed with your question.

Ruplu Bhattacharya
Analyst, Bank of America
Q

Hi, and thanks for taking my questions. Revathi, you talked about strong growth in power and cloud, and I think you guided to 30% year-on-year growth. Can you delve a little bit deeper into who the customer set that you're targeting now for both cloud and power? In cloud, I mean, can you maintain that growth with just the top customer that you had or are you planning to expand beyond that customer? Is hyperscale the customer set or is it enterprise?

And in power, can you give some details on what the customer set is and which region do you see power products growing? Any kind of details to help us get comfortable with the 30% year-on year-growth rate? And I have a follow up. Thank you.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.
A

Yeah, yeah. I'd say, Ruplu, I'd start with saying, one is you should be very comfortable with the 30%, because you have just seen what we have executed in the last few years, right? So that is one thing. And then second, as you all point out to me all the time, is that they're always conservative in kind of what we say, long-term, right, in terms of our guidance. So I would say that 30% is, you should absolutely feel comfortable with.

Now, where is it coming from? I'd say on our IT integration side, I think one of the things that is really important to know what's different about us is, we have multiple hyperscaler customers, right? So, almost all large hyperscaler customers are part of our customer mix. So, we're not really geared towards or targeted towards one large hyperscaler. And they're all growing fairly significantly and have very big long-term programs that are up and coming.

And they're also growing with kind of the smaller cloud customers, who now – now you're are seeing a lot of offsets to also hyperscalers, where there are smaller cloud customers that are coming up in various regions and we are also supporting them. So that is also very significantly important. So, very diversified end customers in our IT integration side.

In the power side, on the embedded power business where we design power that goes on the chip, we mainly work with the silicon providers, because they're the ones who are driving actually what the significant compute requirements that's required. So we start by working with the silicon providers, which in some cases are also hyperscalers who are making their own silicon. And there also, there is pretty significant diversification in terms of end customers.

And in our critical power, we work with almost every large colo and almost every large hyperscaler, mainly in Europe and North America. I'd say we do less in terms of Asia in critical power, but very diversified from a geography and an end customer standpoint.

So, that's what really makes our data center business very unique as a diversification in all these three businesses, which is really important. And then, the critical thing is as technology puts compute and power together, we're the only ones who can really work on that technology in terms of putting that together. So, that's also a very important thing. So...

Ruplu Bhattacharya
Analyst, Bank of America

Q

Okay. Thanks for all the details there, I appreciate that. Can I ask about the customer-sourced inventory and the impact of that on both revenues and margins? I think you talked about a $1 billion impact in fiscal 2026. Is that all in hyperscale or is that in other end markets as well, including – are you seeing that in both the power business as well as in the cloud business? And what is the impact on margins of customers going to a customer-sourced inventory model? Is it positive for margins or negative? Any details would be appreciated. Thank you.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

Yeah, Kevin?

Kevin S. Krumm
Chief Financial Officer, Flex Ltd.

A

Yeah. Hi, Ruplu. I'll take that. Just answering your question. So, your first question on hyperscale, I would say no, it is not isolated. Those contracting arrangements are not isolated to our cloud business, although I would say a majority of the contracts are in the cloud business.

Your question on margins, the short answer is yes, margins get a bump when you look year-on-year. But it's important to note that FY 2025 and as we think about margins as we go into FY 2026, our margins, we do expect our margins to grow without this bump.

Ruplu Bhattacharya
Analyst, Bank of America

Q

Right. Thank you for all the details. Really appreciate it.

Kevin S. Krumm
Chief Financial Officer, Flex Ltd.

A

You're welcome.

Operator: Thank you. Our next question comes from line of George Huang with Barclays. Please proceed with your question.

George Wang
Analyst, Barclays Capital, Inc.

Q

Hey, guys, and thanks for taking my question and congrats on the quarter. I have two quick ones. So firstly, maybe for Kevin. I noticed the implied OPM percentage for 1Q 2026 is a bit lower sequentially, kind of jives with first quarter a year ago as well, kind of a step down from 4Q to 1Q. Is this just due to typical seasonality or kind of startup cost with the program ramping? Can you kind of call out the drivers, kind of pointing to implied OP percentage may be kind of 5.6% for the 1Q?

Kevin S. Krumm
Chief Financial Officer, Flex Ltd.

A

Yeah, hi, George. So, the question on why are implied margins stepping down 4Q 2025 to Q1 2026, I'd say there's really two drivers in there. One is just sequentially our revenue, we expect our revenue to step down. And in some of our business, we're going to have lower fixed cost absorption.

The other thing I would say is, as we go into the first quarter, our automotive business, we're expecting a step down there sequentially Q4 to Q1. And with that and due to the nature of the cost structure in that business, there's going to be a little more margin drag in the first quarter than we would expect as we move through the year there as well. So, those are really your two primary drivers of the step down in operating margin Q4 to Q1.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

And I'd say, George, only thing I'd add to that is, you've seen this in the last year also, right, our Q1 was somewhat soft and had a fairly strong year in terms of our margin performance. And you can see, our FY 2026 guide is really strong, 6% operating margin that we're going to hit a year ahead of schedule. So, I'm not worried about kind of the sequentials. I feel very good about kind of how we have laid this out. It's going to be a strong year.

George Wang
Analyst, Barclays Capital, Inc.

Q

Yeah, yeah, agree. And also, a quick follow-up for Revathi. You guys called out networking share gains, which caught my eye. Just curious if you can double click on the networking share gains. Can you talk about which specific customer set or is mostly broad-based? And in terms of share gains, are these gains from Asia competitors or could be just share gain from US-based EMS guys as well? Just if you can give any color on that. Thanks.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

Yeah. The only thing I would say is, George, is that we mainly grow with kind of large players in the networking space, and they're all fairly well known to you and to everyone. So, we've continued to grow with them in the last few years. And I would say, in terms of geography, it is across the world with these share gains and these customers. So, I think that's all I can add to it, right? I'm not going to share names and all that, but it's a pretty significant part of where we have grown and it's a very good business for us. So...

George Wang
Analyst, Barclays Capital, Inc.

Q

Okay. Just a quick one if I can squeeze in, just in terms of value-added services. Last year, you guys talked about $1 billion. In the prepared remarks, you talked about year-over-year growth. Just curious, any color beyond that, just how to quantify growth rate for FY 2026 for the value-added services, which is margin accretive.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

Yeah. I don't think we are sharing growth rate for FY 2026 in terms of the services business. I think we give you enough as we look back usually on the services business. All I'll say is we expect it to grow again in fiscal 2026 in almost all aspects of that business. As you know very well, it really drives vertical integration for us across multiple end markets. And it is important in terms of how we improve margins, because that is a key part of our strategy.

Revenue-wise, it's not big numbers compared to our overall kind of $25 billion, $26 billion revenue that we have. But really important in terms of building customer affinity and driving margins. But really, no numbers to share for you in terms of exact growth rates and things like that. But we expect it to grow in FY 2026.

George Wang
Analyst, Barclays Capital, Inc.

Q

Great. Thank you. Congrats again on the quarter, guys. I will go back to the queue.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

Thanks, George.

Operator: Thank you. Our next question comes from the line of Mark Delaney with Goldman Sachs. Please proceed with your question.

Mark Delaney
Analyst, Goldman Sachs & Co. LLC

Q

Yes, good morning. Thank you very much for taking my questions. Nice to see the margin strength and recognizing you're guiding to reach the 6% a year earlier than you'd previously targeted. I do want to better understand how tariffs may affect the margin guidance, though. I believe you said, your guidance excludes tariffs both with respect to revenue and cost, and you'd expect tariff cost to be passed through at a low margin. So, if tariff levels are sustained – and I realize tariffs are quite dynamic, but in a scenario where tariff levels are sustained around levels they are today, do you still think you'd be at 6% margins for this coming year?

Kevin S. Krumm
Chief Financial Officer, Flex Ltd.

A

Hi, Mark, this is Kevin. Thanks for the question. I would say – so you're thinking about it the right way. Our guide excludes any direct impacts from tariffs, which would impact both revenue and costs really coming through at flat to zero margin. So, we would expect a drag versus our current guide at margins if tariffs were applied at sort of the current guidance that's out there. We wouldn't expect it to be significant, but there would be some basis points drag versus our current guide.

Mark Delaney
Analyst, Goldman Sachs & Co. LLC

Q

Okay. Thanks for clarifying, Kevin. My other question also related to tariffs and more trying to better understand what kind of knock-on effects tariffs are having to end demand. You said, you're factoring in some weakness into the auto market, but if you think about some of the other end markets, are you seeing any weakness in customer schedules, perhaps if prices are going higher yet you're expecting some negative elasticity of demand. Or if you're not seeing that, is that something you tried to factor into the revenue guidance? Thanks.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

Yeah, I'd say, Mark, we're really not seeing anything in terms of outside of what we have talked about in automotive in any kind of significant weakness in terms of customers itself. And I'll just remind you that if you think about our current business mix, right, even in our lifestyle and consumer end market businesses, we are with kind of really high-end consumers and complex products.

And so, we're not seeing any significant impact there. Of course, our data center business is very strong, we don't see any significant impact there. Industrial businesses, are still holding. As you have seen in terms of CapEx for industrials are still pretty strong, driven by investments that they're making. So, we're not really seeing any significant impact in terms of end market demand outside of automotive.

So, if you think about our guide today, it really reflects that. And you can see that from a lot of the results that are coming out, also that demand is holding pretty well in all the major end markets we're in. So, highly dynamic, of course. Things could change. But I would say both dealing with tariffs pass through and demand, we feel like we have kind of included what we see today in our guide.

Kevin S. Krumm
Chief Financial Officer, Flex Ltd. A

Hey, Mark. The only thing I want to add, because you asked your question based on OP margin, which I understand why you positioned it that way. But when we think about tariffs, while there will be a drag on OP margin, as we've thought about our guide, we do not expect there to be an impact on OP profit dollars this year or EPS dollars for that matter. So I just wanted to clarify that, because that was a critical element of our guide as we thought about it for FY 2026.

Mark Delaney
Analyst, Goldman Sachs & Co. LLC Q

Yeah. No, that makes sense, Kevin. And Revathi, thanks for all your thoughts on what you're seeing by end market.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd. A

Thanks, Mark.

Operator: Thank you. [Operator Instructions] Our next question comes from the line of Steve Barger with KeyBanc Capital Markets. Please proceed with your question.

Christian Zyla
Analyst, KeyBanc Capital Markets, Inc. Q

Good morning. This is Christian Zyla on for Steve Barger. Thanks for taking the questions. First question, just going back to the Husqvarna facility acquisition, could you just give us some additional color on how that deal came about? Was that opportunistic timing or is that business that you were vying for? And then just more broadly, is the current operating environment across the globe getting more potential customers at the table to consider and pursue your entire suite of outsourcing capabilities?

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd. A

Yeah, I would say, Christian, on the deal with Husqvarna, we constantly talk to customers and engage with them about kind of how we can help them with their supply chain, right, so that's a constant conversation with them. As this whole regionalization conversation has become stronger and stronger and we're looking to build our footprint in North America, this was a really good opportunistic deal for us and for the customer where we're able to take on their capability and then add to our footprint and our capability in a region that we are very interested in growing more aggressively.

So, it was really a win-win for us. And more and more conversations like that with customers are happening, where not only can we help them with their footprint, existing footprint, but we can expand our capability with that, too. So, it was a perfect deal, perfect timing, and really excited to welcome that that group into our fold and looking to expand that capability pretty well.

What was the second question? Christian, can you repeat your second question?

Christian Zyla
Analyst, KeyBanc Capital Markets, Inc.

Q

Yes, absolutely. Just is it getting more customers to the table to consider outsourcing or your entire suite of outsourcing capabilities?

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

I'd say, we're getting a lot of customer conversations with our teams in terms of regionalization, but also as you're doing regionalization, taking on more end-to-end capability. Because the hardest part about regionalization is going to be, where is your raw material coming from, who's going to be making that? Everything that's vertically down, not just the final test and assembly. So the better for customers if they handle where things do us more end-to-end, everything from a planning perspective, managing their supply chain to then vertically integrating it into all the aspects that go into the final product, does make it easier for them.

So, we're seeing more of those conversations. It is pushing us to develop our own capability even further in markets like Mexico and in the US, but also develop our supply chain even more aggressively. So, Christian, you're right, it is driving more end-to-end conversations at a faster speed today than it's ever been before.

Christian Zyla
Analyst, KeyBanc Capital Markets, Inc.

Q

That's great. And then if I could just sneak in my second question, it's a follow up on the earlier inventory question. I know in the last few years you guys have been working to bring down the inventory levels, but if we were to see inflection sooner in, say, core Agility or auto markets, should we expect to see an equal uptick in inventories or anything on the working capital side? Just help us think about the inflection and kind of the future. Thank you.

Kevin S. Krumm
Chief Financial Officer, Flex Ltd.

A

Hi. This is Kevin. I'll take that. I mean, sure, when you think about our inventory, to the extent that we see a significant pivot in growth, you would see some investment in our working capital rate as we need that – sorry, working capital, not working capital rate, but we would need that investment to support growth in our model.

All that said, there will continue to be opportunity in working capital rate that would offset that investment. So, yes, as we pivot to growth, you asked on automotive, but I would say this across all of our SBUs, you would see some working capital investment. But we have rate opportunity we're going to continue to work on, and that's going to help offset some of that investment as we go forward here.

Revathi Advaithi
Chief Executive Officer & Director, Flex Ltd.

A

Yeah. The only thing I would add, Kevin, to that is, one thing we learned through the supply chain crisis is getting really good in terms of managing inventory end-to-end, right, so not just for us but for our customers and then through the supply chain. So, all of those learnings and systems and processes we have developed, will all come into play as overall at the end of the day, we want to make sure our days are well in control for us and our customers. So yes, we'll need more inventory to support growth, but the important part is we will manage our days of inventory really well across the supply chain.

Christian Zyla
Analyst, KeyBanc Capital Markets, Inc.

Q

Thank you, guys.

Kevin S. Krumm
Chief Financial Officer, Flex Ltd.

A

Thank you.

Operator: Thank you. Ladies and gentlemen, this concludes our question-and-answer session and thus concludes our call today. We thank you for your interest and participation. You may now disconnect your lines.