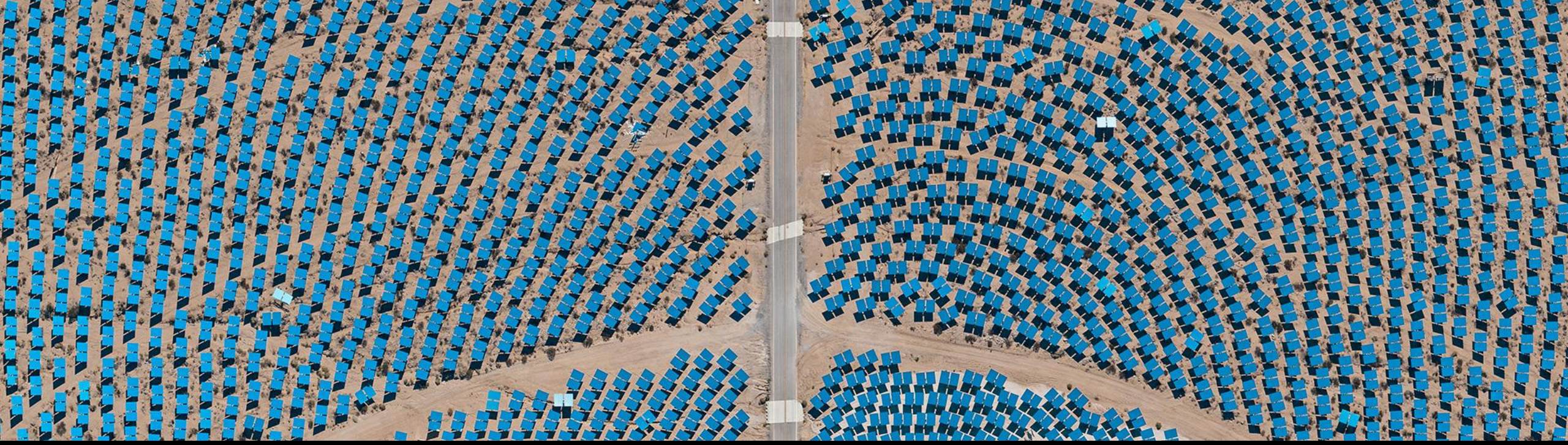


CFO Commentary

Third Quarter 2023

investor.arrow.com

CFO Commentary

As reflected in our earnings release, there are a number of items that impact the comparability of our results with those in the trailing quarter and prior-year comparable periods. The discussion of our results may exclude these items to give you a better sense of our operating results. As always, the operating information we provide to you should be used as a complement to, and not in substitute for, GAAP numbers. For a complete reconciliation between our GAAP and non-GAAP results, please refer to our third quarter 2023 Form 10-Q, earnings release and the earnings reconciliation found at the end of this document.

The following reported GAAP and non-GAAP information included in this CFO commentary is unaudited and should be read in conjunction with the company's Form 10-Q for the quarterly period ended September 30, 2023, and the company's 2022 Annual Report on Form 10-K, each as filed with the Securities and Exchange Commission.



Third-Quarter Summary

Third-quarter 2023 sales were $8.01 billion, a decrease of 14 percent year on year. Third-quarter net income was $199 million, or $3.53 per share on a diluted basis, compared with net income of $342 million, or $5.27 per share on a diluted basis, in the third quarter of 2022. Non-GAAP net income was $233 million, or $4.14 per share on a diluted basis, in the third quarter of 2023, compared with non-GAAP net income of $354 million, or $5.45 per share on a diluted basis, in the third quarter of 2022.

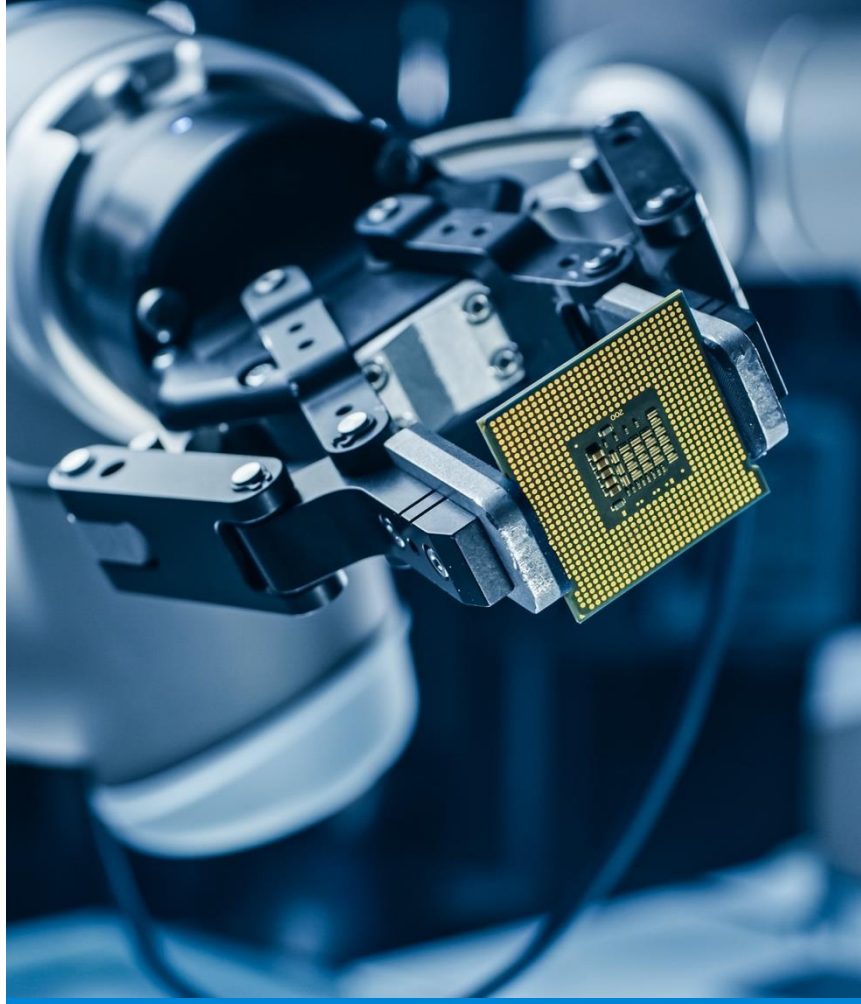
Both GAAP and non-GAAP earnings per share in the third quarter of 2023 included a $0.87 benefit related to cash received from a legal settlement in the global components business, and a $0.31 impact for a charge taken to increase accounts receivable reserves associated with a customer in the global enterprise computing solutions (ECS) business.

The company executed well amidst an inventory correction in the semiconductor market and a softer information technology market.

In our global components business, with lead times further improving, customer inventory remained elevated, impacting order velocity and top line results across most vertical markets. Despite the market conditions, operating margins are meaningfully higher than in prior market corrections. We were encouraged by the level of demand creation activity in the quarter and the continued traction of our supply chain services offering.

The mix in our ECS business continued to shift toward software related to infrastructure and cybersecurity, as well as cloud solutions. As a result, the business produced year-on-year billings growth albeit with a decline in net sales.

Non-GAAP earnings per share after adjusting for the legal settlement and accounts receivable item, was at the high end of our guidance range. We were pleased to generate $322 million in cash flow from operations in the third quarter. Additionally, we repurchased approximately $200 million of shares during the third quarter and now have remaining purchase authorization of approximately $622 million.



Consolidated Overview

Third Quarter 2023

P&L Highlights*	Q3 2023	Y/Y CHANGE	Y/Y CHANGE IN CONSTANT CURRENCY	Q/Q CHANGE
Sales	$8,007	(14)%	(15)%	(6)%
Gross Profit Margin	12.2%	-60 bps	-60 bps	-30 bps
Operating Income	$340	(32)%	(33)%	(13)%
Operating Margin	4.2%	-120 bps	-120 bps	-40 bps
Non-GAAP Operating Income	$379	(26)%	(27)%	(8)%
Non-GAAP Operating Margin	4.7%	-90 bps	-90 bps	-10 bps
Net Income	$199	(42)%	(43)%	(16)%
Diluted EPS	$3.53	(33)%	(34)%	(14)%
Non-GAAP Net Income	$233	(34)%	(35)%	(7)%
Non-GAAP Diluted EPS	$4.14	(24)%	(25)%	(5)%

** $ in millions, except per share data; may reflect rounding.*

Third-quarter diluted EPS of $3.53 and non-GAAP diluted EPS of $4.14

Consolidated sales were $8.01 billion

In line with the prior expectation of $7.78-$8.38 billion

Consolidated gross profit margin was 12.2%

Down 60 basis points year on year primarily due to lower margins in global components

Declined 30 basis points compared to the second quarter of 2023

Operating income margin was 4.2% and non-GAAP operating income margin was 4.7%

Operating margin in the third quarter of 2023 included an 80bps benefit related to cash received from a legal settlement in the global components business, and a 30bps impact for a charge taken to increase accounts receivable reserves associated with a customer in the ECS business.

Interest and other expense, net was $82 million

Below our prior expectation of approximately $85-$90 million due to lower average daily balances

Third Quarter 2023

Effective tax rate was 20.7%, and non-GAAP effective tax rate was 21.2%

Effective tax rate and non-GAAP effective tax rate were below the prior expectation and the target long-term range of 23% - 25% as a result of utilizing certain domestic and foreign tax credits

Diluted earnings per share were $3.53

Average diluted shares outstanding were 56 million

In line with the prior expectation

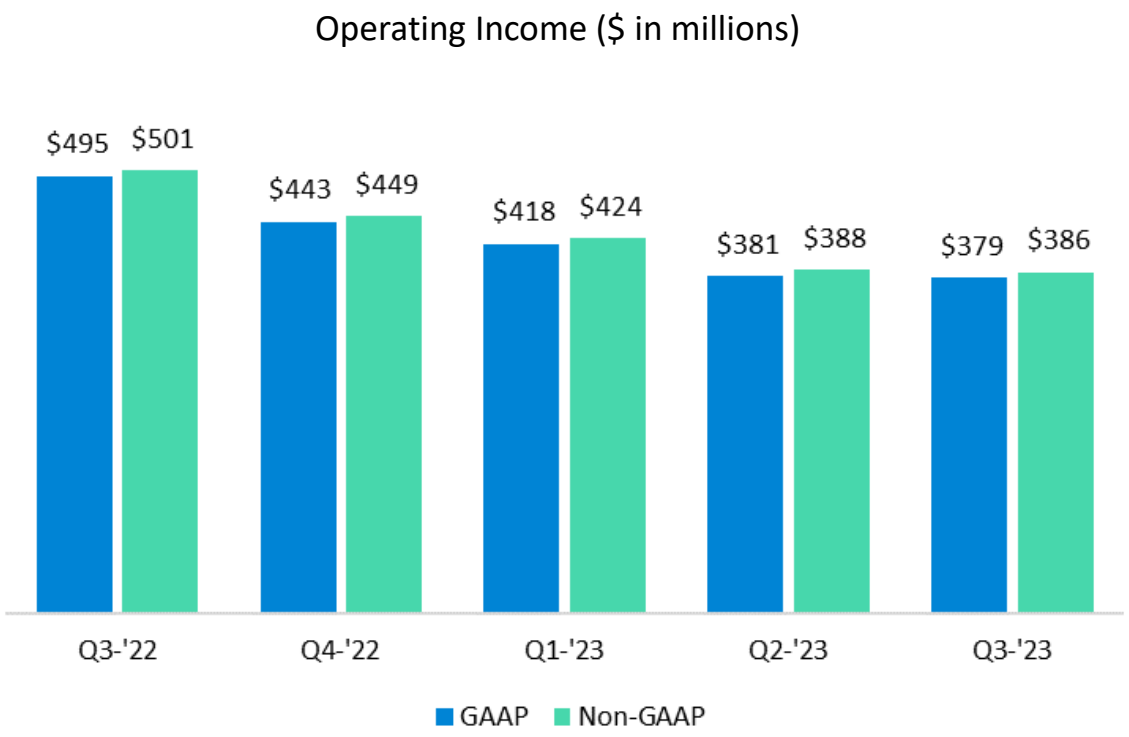
Non-GAAP diluted earnings per share were $4.14

Better than the prior expectation of $3.40 - $3.60. Includes $0.87 benefit related to cash received from a legal settlement in the global components business, and a $0.31 impact for a charge taken to increase accounts receivable reserves associated with a customer in the ECS business.



Components

Global



Third-quarter sales decreased 14% year on year

Third-quarter sales decreased 14% year on year

Lead times have normalized

Book to bill was below parity but has remained steady

Sales of $6.25 billion were slightly better than the midpoint of prior expectation of $6.2 billion

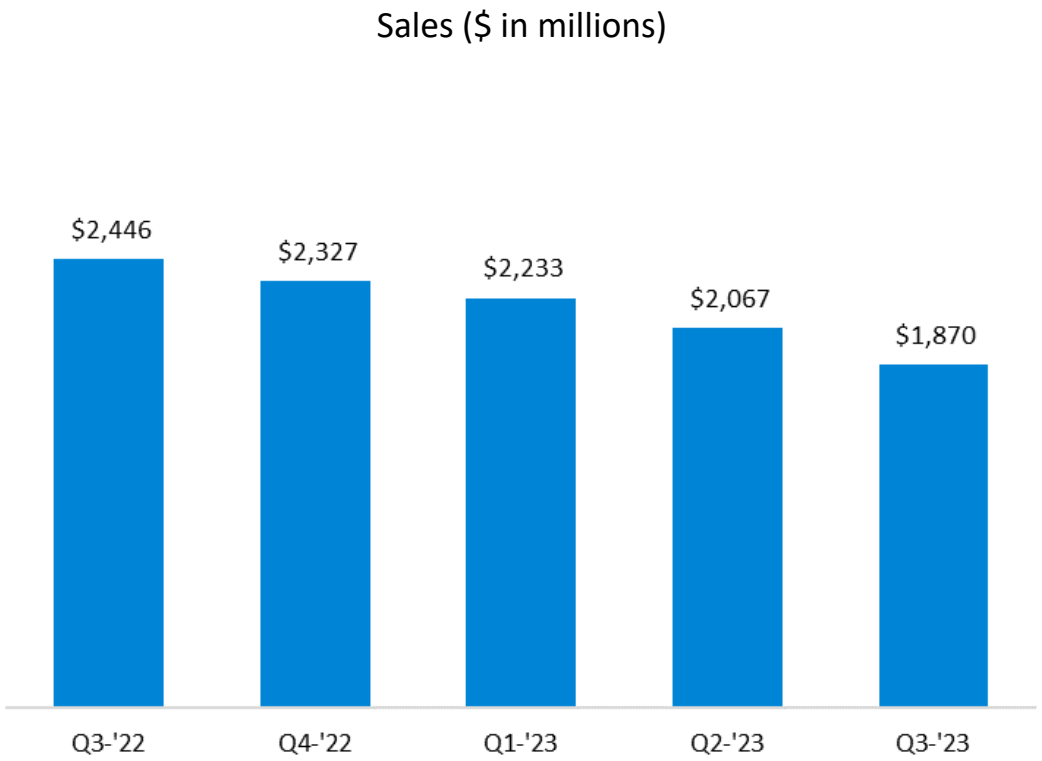
Operating margin of 6.1% decreased 70 basis points year on year primarily due to reduced volumes in the component shortage market in the Americas

Non-GAAP operating margin of 6.2% decreased 70 basis points year on year

Global component operating margins benefited 100 bps from a $62 million legal settlement

Components

Americas



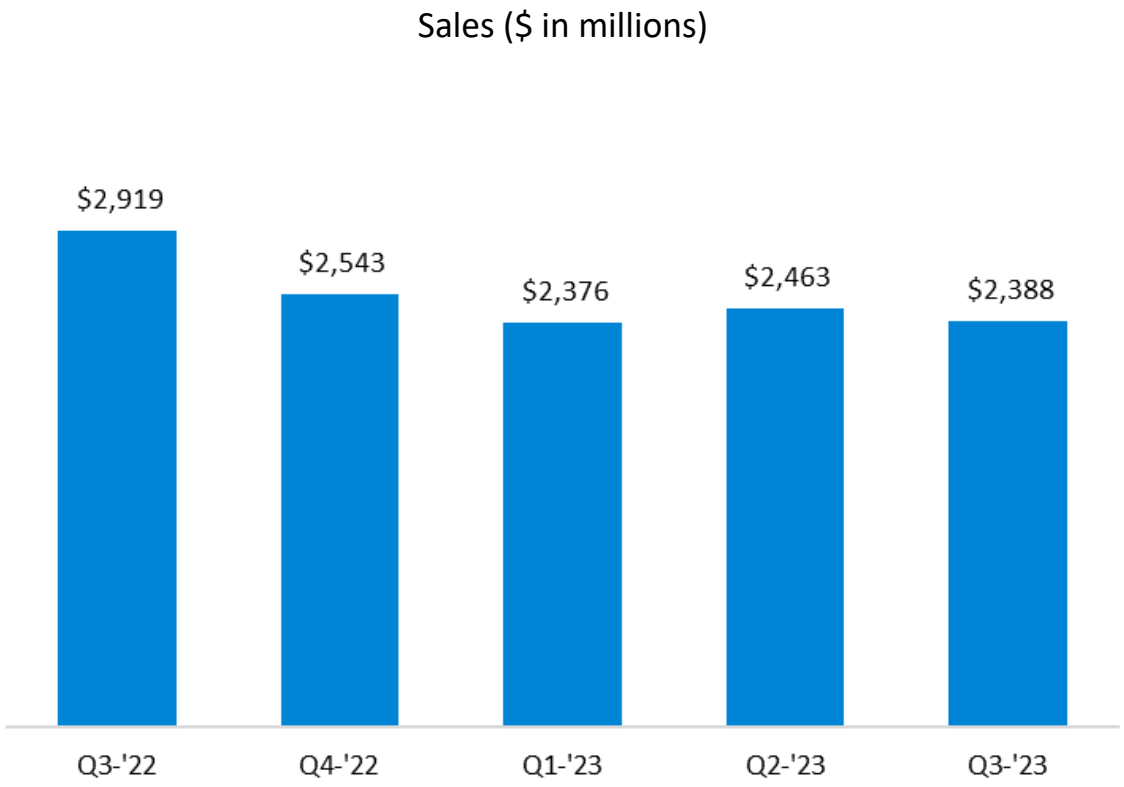
Third-quarter sales decreased 24% year on year

As expected, the year on year decline in revenue is primarily a function of the normalization of shortage market activities

Strength in aerospace and defense verticals

Components

Asia

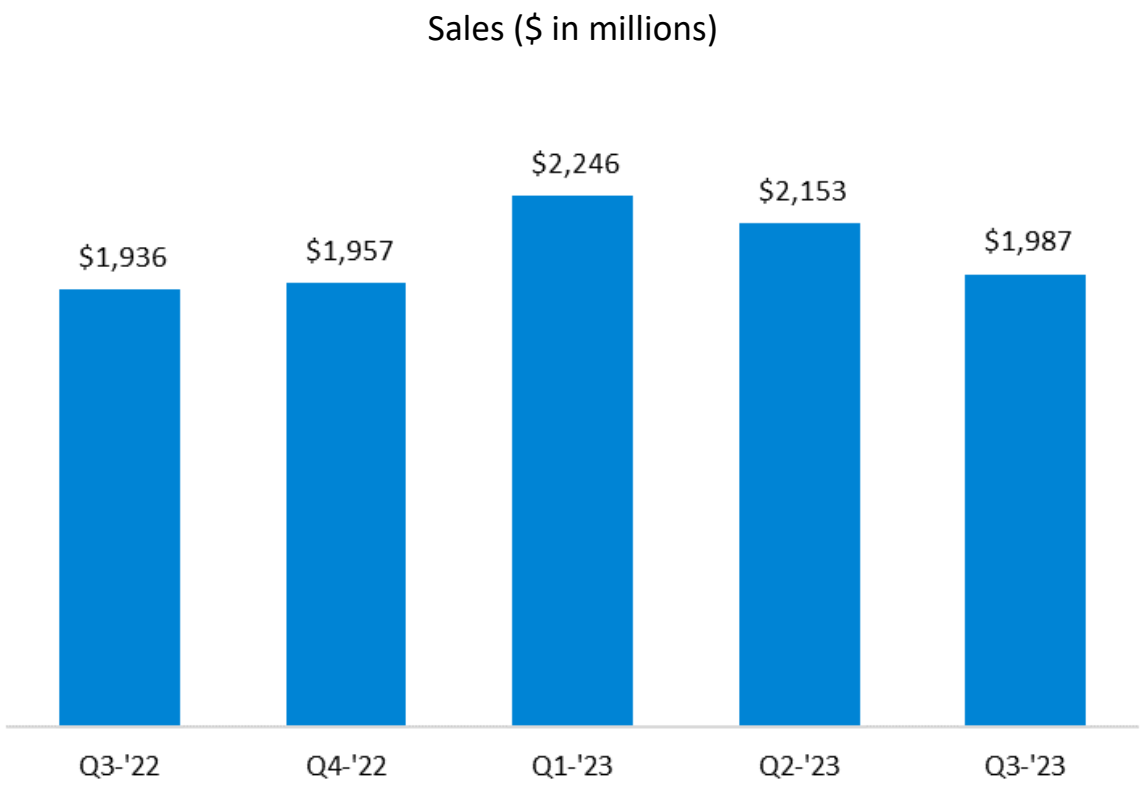


Third-quarter sales decreased 18% year on year

Continued softness across the region

Components

Europe



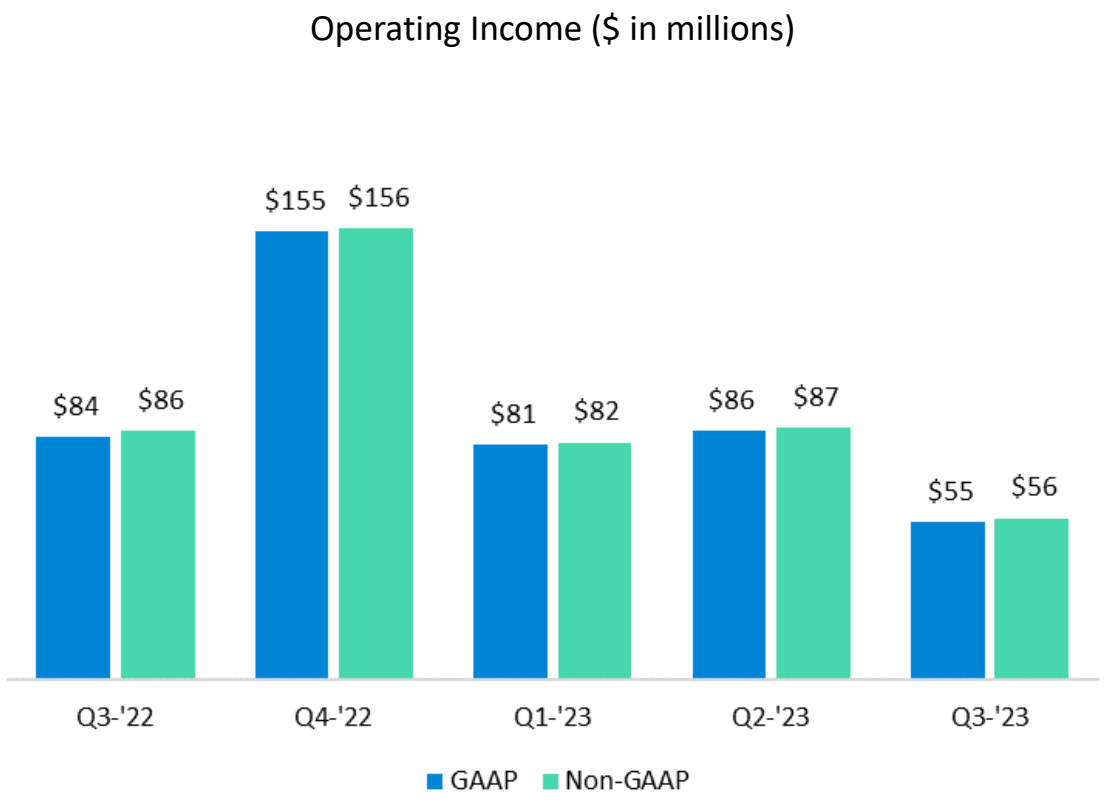
Third-quarter sales increased 3% year on year

Improvement in interconnects, passives & electromechanical orders

Strength in industrial, automotive and aerospace & defense

Enterprise Computing Solutions

Global



Third-quarter sales decreased 10% year on year

Third-quarter sales decreased 10% year on year

Operating income decreased 35% year on year and includes a $22 million impact for a charge taken to increase accounts receivable reserves associated with a customer

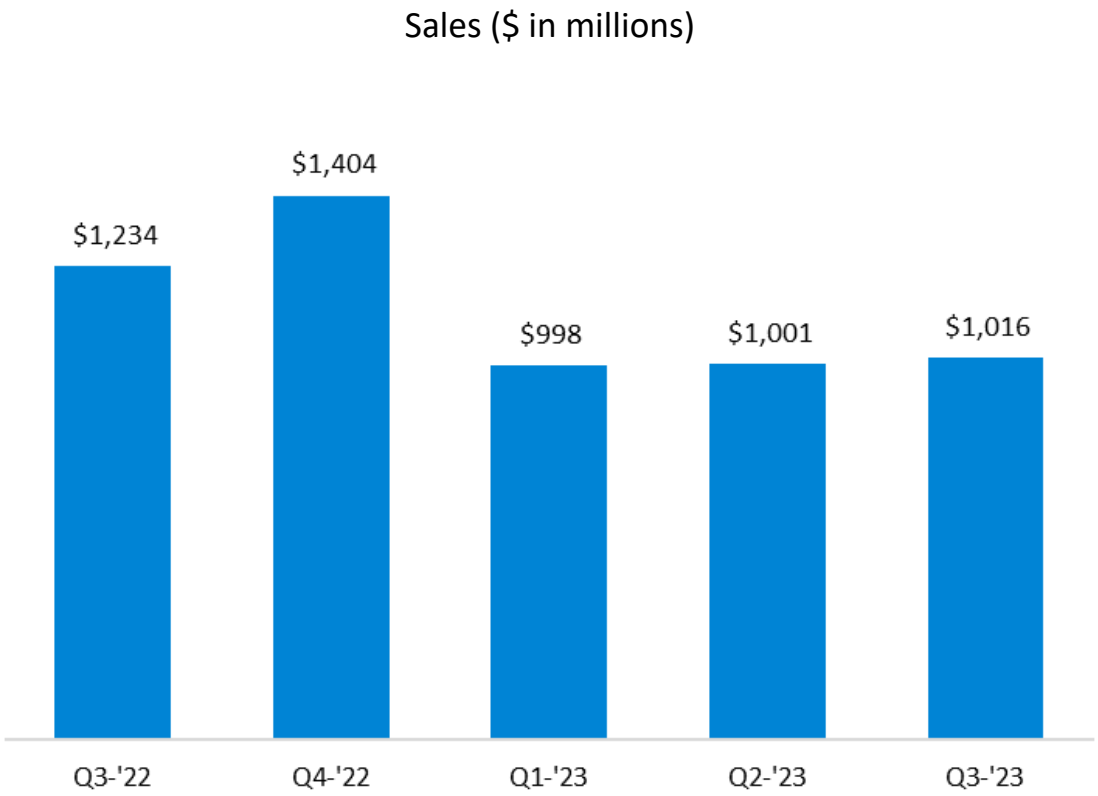
Relative strength in cloud, software, and services as customers migrate to IT solutions delivered on an as-a-service basis

Operating margin of 3.1% decreased 120 bps year on year due to the 120 bps impact for a charge taken to increase accounts receivable reserves associated with a customer

Non-GAAP operating margin of 3.2% decreased 120 bps year on year due to the 120 bps impact for a charge taken to increase accounts receivable reserves associated with a customer

Enterprise Computing Solutions

Americas

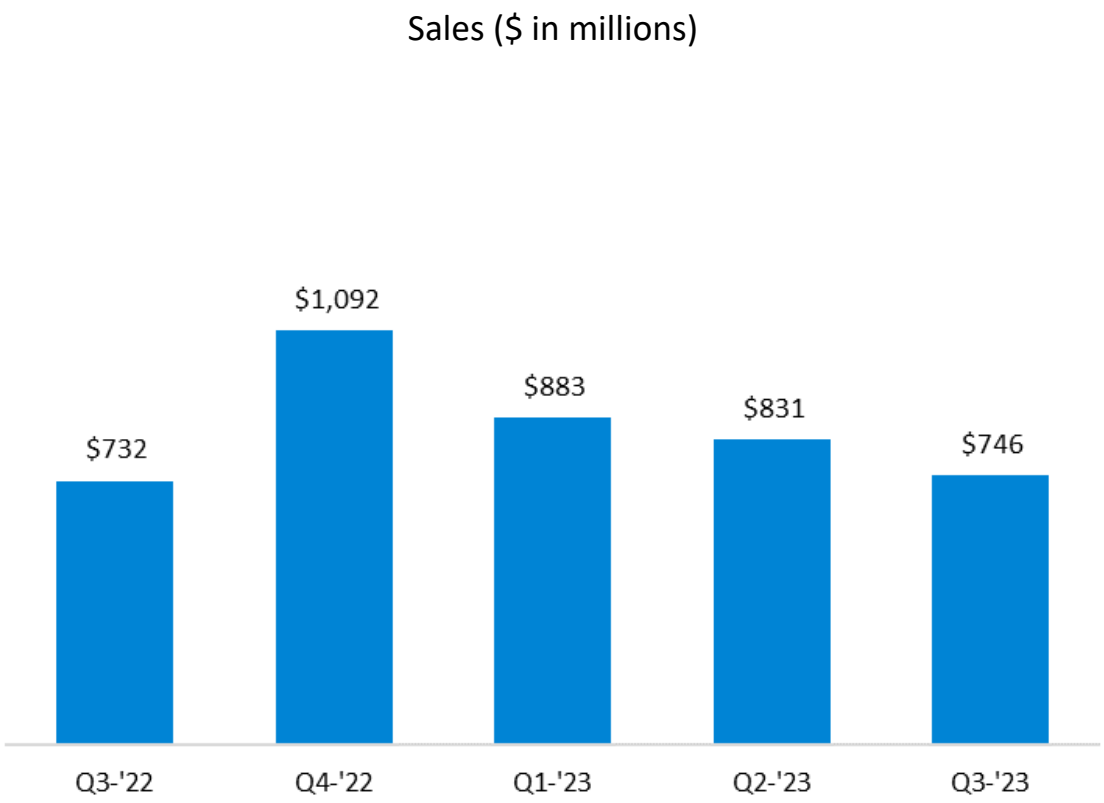


Third-quarter sales decreased 18% year on year

Relative strength in the public sector

Enterprise Computing Solutions

Europe



Third-quarter sales increased 2% year on year

Healthy demand for cyber-security solutions and other infrastructure software

Cash Flow, Returns, and Liquidity

Third Quarter 2023

Cash Flow from Operations
Cash flow provided by operating activities was $322 million in the third quarter and cash provided by operating activities was $419 million year-to-date.

Working Capital
The company reports return on working capital ("ROWC") and ROWC (non-GAAP) to provide investors an additional method for assessing working capital. The company uses ROWC to measure economic returns to help the company evaluate the effectiveness of investments in the inventories we chose to buy and the business arrangements we have with our customers and suppliers. ROWC was 18.4% in the third quarter, down 1130 basis points year on year. ROWC (non-GAAP) was 20.6% in the third quarter, down 990 basis points year on year. The decrease in ROWC related primarily to lower operating income due to normalizing market conditions, in addition to higher inventory levels. See pg. 19 for the company's calculation of ROWC.

Return on Invested Capital
The company reports return on invested capital ("ROIC") and ROIC (non-GAAP) to provide investors an additional method for assessing operating income. Among other uses, the company uses ROIC to measure economic returns relative to our cost of capital in evaluating overall effectiveness of our business strategy. ROIC was 11.3% in the third quarter, down 640 basis points year on year. ROIC (non-GAAP) was 12.6% in the third quarter, down 550 basis points year on year. The decrease in ROIC related primarily to higher levels of debt, primarily related to investments in inventory, as well as lower operating income. See pg. 20 for the company's calculation of ROIC.

Share Buyback
We repurchased 1.6 million shares for approximately $200 million in the third quarter of 2023. Total remaining repurchase authorization is $622 million.

Debt and Liquidity
Net debt totaled $3.9 billion. Total liquidity was $2.3 billion when including cash of $333 million.



Repurchased approximately $200 million of stock in the third quarter.

Outlook: Fourth Quarter 2023

Guidance

We estimate changes in foreign currencies to increase year-over-year growth in sales by $54 million and earnings per share on a diluted basis by $0.02 compared to the fourth quarter of 2022. We estimate changes in foreign currencies to decrease quarter-over-quarter growth in sales by $82 million and earnings per share on a diluted basis by $0.07 compared to the third quarter of 2023(1).

Fourth-Quarter 2023 Guidance

Consolidated Sales	$7.50 billion to $8.10 billion
Global components	$5.40 billion to $5.80 billion
Global ECS	$2.10 billion to $2.30 billion
Diluted Earnings Per Share*	$3.30 to $3.50
Non-GAAP Diluted Earnings Per Share*	$3.61 to $3.81
Interest and other expense, net	Approximately $90 million
Diluted shares outstanding	~55 million

* Assumes an average tax rate in the range of 23% to 25%.

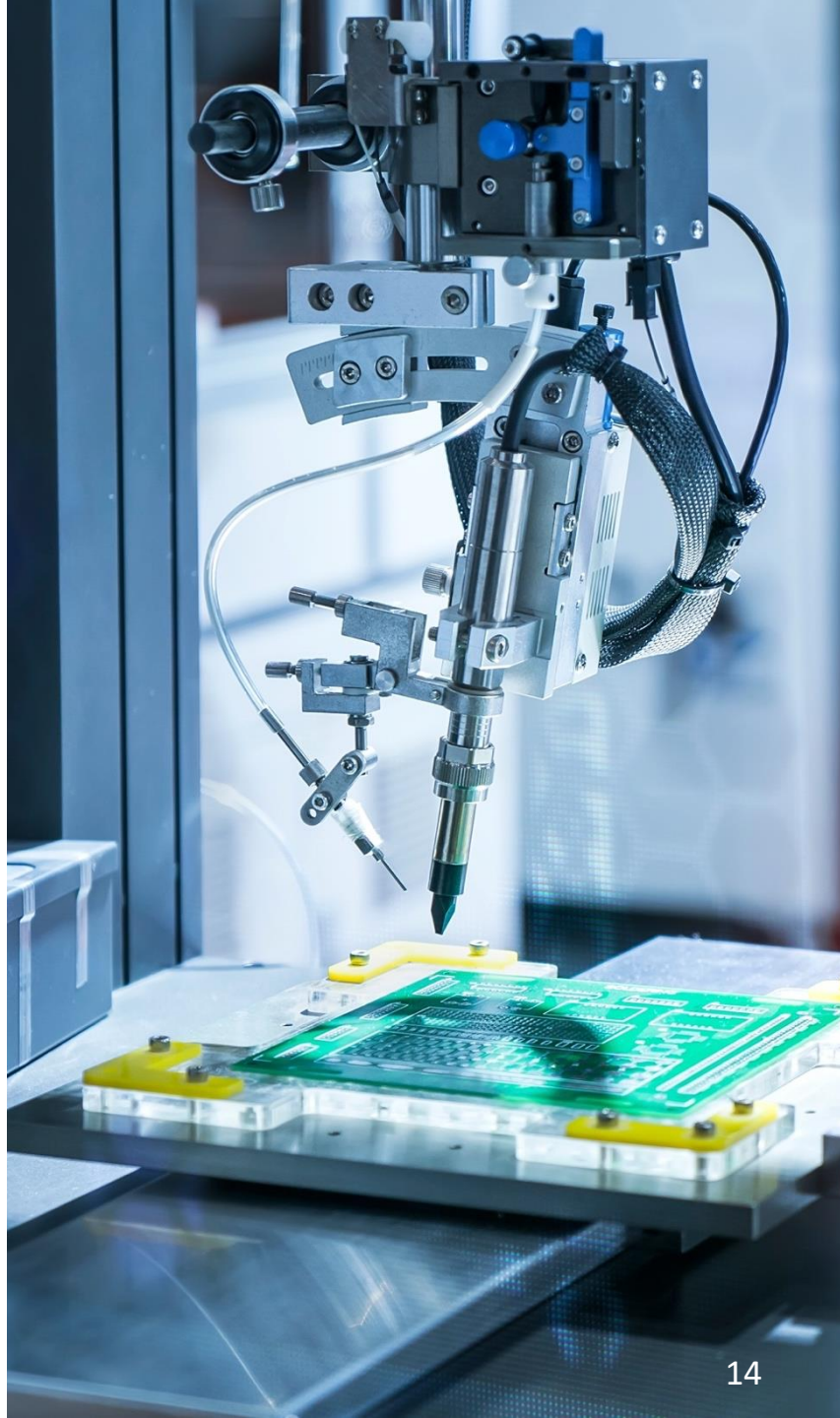
On a constant currency basis(1), our fourth-quarter sales guidance implies a sequential growth rate range of down 13% to down 6% for global components and up 21% to up 32% for global enterprise computing solutions, when compared to the third-quarter of 2023.

Quarter Closing Dates

Beginning and ending dates may impact comparisons to prior periods

	First	Second	Third	Fourth
2022	Apr. 2	Jul. 2	Oct. 1	Dec. 31
2023	Apr. 1	Jul. 1	Sep. 30	Dec. 31

(1) Refer to p.17 of this presentation for fourth quarter 2023 GAAP to non-GAAP Outlook Reconciliation.



Risk factors

The discussion of the company's business and operations should be read together with the risk factors contained in Item 1A of its most recent Annual Report on Form 10-K and each subsequently filed Quarterly Report on Form 10-Q, filed with the Securities and Exchange Commission, which describe various risks and uncertainties to which the company is or may become subject. If any of the described events occur, the company's business, results of operations, financial condition, liquidity, or access to the capital markets could be materially adversely affected.

Information Relating to Forward-Looking Statements

This presentation includes "forward-looking" statements, as the term is defined under the federal securities laws, including but not limited to statements regarding: Arrow's future financial performance, including its outlook on financial results for the fourth quarter of fiscal 2023 such as sales, net income per diluted share, non-GAAP net income per diluted share, average tax rate, average diluted shares outstanding, interest and other expense, impact to sales due to changes in foreign currencies, intangible amortization expense per diluted share, restructuring & integration charges per diluted share, and expectations regarding market demand and shareholder returns. These and other forward-looking statements are subject to numerous assumptions, risks, and uncertainties, which could cause actual results or facts to differ materially from such statements for a variety of reasons, including, but not limited to: unfavorable economic conditions; disruptions or inefficiencies in the supply chain; political instability; impacts of military conflict and sanctions; industry conditions; changes in product supply, pricing and customer demand; competition; other vagaries in the global components and the global ECS markets; deteriorating economic conditions, including economic recession, inflation, tax rates, foreign currency exchange rates, or the availability of capital; the effects of natural or man-made catastrophic events; changes in relationships with key suppliers; increased profit margin pressure; changes in legal and regulatory matters; non-compliance with certain regulations, such as export, antitrust, and anti-corruption laws; foreign tax and other loss contingencies; outbreaks, epidemics, pandemics, or public health crises; and the company's ability to generate positive cash flow. For a further discussion of these and other factors that could cause the company's future results to differ materially from any forward-looking statements, see the section entitled "Risk Factors" in the company's most recent Quarterly Report on Form 10-Q and the company's most recent Annual Report on Form 10-K, as well as in other filings the company makes with the Securities and Exchange Commission. Shareholders and other readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date on which they are made. The company undertakes no obligation to update publicly or revise any of the forward-looking statements.

Certain Non-GAAP Financial Information

In addition to disclosing financial results that are determined in accordance with accounting principles generally accepted in the United States (“GAAP”), the company also provides certain non-GAAP financial information. The company provides non-GAAP sales, operating expenses, operating income, operating income margin, income before income taxes, provision for income taxes, consolidated net income, noncontrolling interests, net income attributable to shareholders, effective tax rate, net income per share on a diluted basis, return on working capital, and return on invested capital.

These non-GAAP measures are adjusted by certain of the following, as applicable: the impact of changes in foreign currencies (referred to as "changes in foreign currencies" or "on a constant currency basis") by re-translating prior-period results at current period foreign exchange rates, identifiable intangible asset amortization, restructuring, integration, and other charges, net gains and losses on investments, and impact of tax legislation changes.

Management believes that providing this additional information is useful to the reader to better assess and understand the company’s operating performance and future prospects in the same manner as management, especially when comparing results with previous periods. Management typically monitors the business as adjusted for these items, in addition to GAAP results, to understand and compare operating results across accounting periods, for internal budgeting purposes, for short- and long-term operating plans, and to evaluate the company's financial performance. However, analysis of results on a non-GAAP basis should be used as a complement to, in conjunction with, and not as a substitute for, data presented in accordance with GAAP.

For a complete reconciliation between our GAAP and non-GAAP results, please refer to our third quarter 2023 Form 10-Q, earnings release and the earnings reconciliations found at the end of this document.



The company believes that such non-GAAP financial information is useful to investors to assist in assessing and understanding the company’s operating performance.

Fourth-Quarter 2023 GAAP to non-GAAP Outlook Reconciliation

($ in billions, except per share data)

NON-GAAP SALES RECONCILIATION

	Quarter Ended			Quarter Ended		
	31-Dec-23	31-Dec-22	% Change	31-Dec-23	30-Sep-23	% Change
Global components sales, GAAP	$5.40 - 5.80	$ 6.83	(21%) - (15%)	$5.40 - 5.80	$ 6.25	(14%) - (7%)
Impact of changes in foreign currencies	—	0.03		—	(0.06)	
Global components sales, constant currency	$5.40 - 5.80	$ 6.86	(21%) - (15%)	$5.40 - 5.80	$ 6.19	(13%) - (6%)
Global ECS sales, GAAP	$2.10 - 2.30	$ 2.50	(16%) - (8%)	$2.10 - 2.30	$ 1.76	19% - 31%
Impact of changes in foreign currencies	—	0.02		—	(0.02)	
Global ECS sales, constant currency	$2.10 - 2.30	$ 2.52	(17%) - (9%)	$2.10 - 2.30	$ 1.74	21% - 32%

NON-GAAP EARNINGS RECONCILIATION

	REPORTED GAAP MEASURE	INTANGIBLE AMORTIZATION EXPENSE	RESTRUCTURING & INTEGRATION CHARGES	NON-GAAP MEASURE
Net income per diluted share	$3.30 to $3.50	$0.10	$0.21	$3.61 to $3.81

Earnings Reconciliation

($ in thousands, except per share data)

Three months ended September 30, 2023

	Reported GAAP measure	Intangible Amortization Expense	Restructuring & Integration charges [1]	Non- recurring tax items	Other [2]	Non-GAAP measure
Operating income	$ 340,083	$ 7,863	$ 31,359	$ -	$ -	$ 379,305
Income before income taxes	252,282	7,863	31,359	-	6,159	297,663
Provision for income taxes	52,241	1,959	7,321	-	1,476	62,997
Consolidated net income	200,041	5,904	24,038	-	4,683	234,666
Noncontrolling interests	1,382	138	-	-	-	1,520
Net income attributable to shareholders	$ 198,659	$ 5,766	$ 24,038	$ -	$ 4,683	$ 233,146
Net income per diluted share [3]	$ 3.53	$ 0.10	$ 0.43	$ -	$ 0.08	$ 4.14
Effective tax rate [4]	20.7%					21.2%

Three months ended October 1, 2022

	Reported GAAP measure	Intangible Amortization Expense	Restructuring & Integration charges [1]	Non- recurring tax items	Other [2]	Non-GAAP measure
Operating income	$ 502,694	$ 8,674	$ 3,635	$ -	$ -	$ 515,003
Income before income taxes	449,106	8,674	3,635	-	3,480	464,895
Provision for income taxes	105,500	2,219	892	-	841	109,452
Consolidated net income	343,606	6,455	2,743	-	2,639	355,443
Noncontrolling interests	1,207	125	-	-	-	1,332
Net income attributable to shareholders	$ 342,399	$ 6,330	$ 2,743	$ -	$ 2,639	$ 354,111
Net income per diluted share [3]	$ 5.27	$ 0.10	$ 0.04	$ -	$ 0.04	$ 5.45
Effective tax rate [4]	23.5%					23.5%

Three months ended July 1, 2023

	Reported GAAP measure	Intangible Amortization Expense	Restructuring & Integration charges [1]	Non- recurring tax items	Other [2]	Non-GAAP measure
Operating income	$ 392,250	$ 7,908	$ 10,333	$ -	$ -	$ 410,491
Income before income taxes	310,171	7,908	10,333	-	(497)	327,915
Provision for income taxes	72,380	1,992	2,597	(942)	(119)	75,908
Consolidated net income	237,791	5,916	7,736	942	(378)	252,007
Noncontrolling interests	1,232	136	-	-	-	1,368
Net income attributable to shareholders	$ 236,559	$ 5,780	$ 7,736	$ 942	$ (378)	$ 250,639
Net income per diluted share [3]	$ 4.12	$ 0.10	$ 0.13	$ 0.02	$ (0.01)	$ 4.37
Effective tax rate [4]	23.3%					23.1%

(1) Includes charges to increase the environmental remediation reserves in the amount of $20.9 million and for third quarter of 2023, $1.9 million for the third quarter of 2022, and $2.4 million for the second quarter of 2023.

(2) Other includes (gain) loss on investments, net.

(3) The sum of the components for non-GAAP diluted EPS may not agree to totals, as presented, due to rounding.

(4) The items as shown in this table, represent the reconciling items for the tax rate as reported by GAAP measure and as a non-GAAP measure.

Return on Working Capital Reconciliation

($ in thousands)

	Quarter Ended	
	September 30, 2023	October 1, 2022
Numerator:	(unaudited)	(unaudited)
Consolidated operating income, as reported	$ 340,083	$ 502,694
	x 4	x 4
Annualized consolidated operating income	$ 1,360,332	$ 2,010,776
Non-GAAP consolidated operating income	$ 379,305	$ 515,003
	x 4	x 4
Annualized non-GAAP consolidated operating income	$ 1,517,220	$ 2,060,012
Denominator:		
Accounts receivable, net	$ 10,663,164	$ 11,218,611
Inventories	$ 5,805,520	$ 5,083,378
Less: Accounts payable	$ 9,090,554	$ 9,540,449
Working capital	$ 7,378,130	$ 6,761,540
Return on working capital	18.4%	29.7%
Return on working capital (Non-GAAP)	20.6%	30.5%

Return on Invested Capital Reconciliation

($ in thousands)

	Quarter Ended	
	September 30, 2023	October 1, 2022
Numerator:		
Consolidated operating income, as reported	$ 340,083	$ 502,694
Equity in earnings of affiliated companies [(1)]	1,392	1,718
Less: Noncontrolling interests [(1)]	1,382	1,207
Consolidated operating income, as adjusted	340,093	503,205
Less: Tax effect [(2)]	70,704	118,497
After-tax consolidated operating income, as adjusted	269,389	384,708
	x 4	x 4
Annualized after-tax consolidated operating income, as adjusted	$ 1,077,556	$ 1,538,832
Non-GAAP consolidated operating income	$ 379,305	$ 515,003
Equity in earnings of affiliated companies [(1)]	1,392	1,718
Less: Noncontrolling interests [(1)]	1,520	1,332
Non-GAAP consolidated operating income, as adjusted	379,177	515,389
Less: Tax effect [(3)]	80,600	121,631
After-tax non-GAAP consolidated operating income, as adjusted	298,577	393,758
	x 4	x 4
Annualized after-tax non-GAAP operating income, as adjusted	$ 1,194,308	$ 1,575,032
Denominator:		
Average short-term borrowings, including current portion of long-term debt [(4)]	$ 1,038,415	$ 615,285
Average long-term debt [(4)]	3,143,915	3,021,758
Average total equity [(4)]	5,603,974	5,350,485
Average cash and cash equivalents	286,838	279,790
Invested capital	$ 9,499,466	$ 8,707,738
Return on invested capital	11.3%	17.7%
Return on invested capital (Non-GAAP)	12.6%	18.1%

(1) Operating income, as reported, and non-GAAP operating income is adjusted for noncontrolling interest and equity in earnings of affiliated companies to include the pro-rata ownership of non-wholly owned subsidiaries.

(2) The tax effect is calculated by applying the effective tax rate for the three months ended September 30, 2023 and October 1, 2022 to consolidated operating income, as adjusted. The tax rate is adjusted to exclude the impacts of interest expense, gain (loss) on investments, net, and employee benefit plan expense, net.

(3) The tax effect is calculated by applying the non-GAAP effective tax rate for the three months ended September 30, 2023 and October 1, 2022 to non-GAAP consolidated operating income, as adjusted. The tax rate is adjusted to exclude the impacts of interest expense and employee benefit plan expense, net.

(4) The quarter ended average is based on the addition of the account balance at the end of the most recently-ended quarter to the account balance at the end of the prior quarter and dividing by two.