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PRESENTATION

Operator

Good morning, and welcome to the Sensata third-quarter 2016 earnings conference call. At this time, I would like to inform you that this call is being recorded.

For opening remarks and introductions, I would like to turn the call over to Joshua Young, Vice President of Investor Relations. Mr. Young, you may begin.

Joshua Young - *Sensata Technologies Holding N.V. - VP of IR*

Thank you, Beth, good morning and welcome to Sensata's third-quarter 2016 earnings conference call. At this time, I'd like to inform you that this call is being recorded. As we begin the call today, joining me on the call will be Martha Sullivan, Sensata's President and CEO; and Paul Vasington, Sensata's Chief Financial Officer.

In addition to the Earnings Release we issued earlier today, we will be referencing a slide presentation during today's conference call. The PDF of this presentation can be downloaded from Sensata's investor relations website. We will also post a replay of today's webcast, shortly after conclusion of today's call.

Before we begin, I'd like to reference Sensata's Safe Harbor statement on slide number 2. During the course of this conference call, we will make forward-looking statements regarding future events or the financial performance of the Company that involved risks and uncertainties. The

Company's actual results may differ materially from the projections described in such statements. Factors that might cause such differences include, but are not limited to, those discussed in our Forms 10-Q and 10-K, as well as other subsequent filings with the SEC.

On slide number 3, I show Sensata's GAAP P&L for the third quarter of 2016. We encourage you to review our GAAP financial statements as part of today's presentation. Most of the subsequent information that we will discuss during today's call will be related to non-GAAP financial measures. A reconciliation for each of our GAAP to non-GAAP financial measures is included in our earnings release and in our webcast presentation.

Martha will begin today's call with an overall business summary, Paul will then cover our financials for the third-quarter 2016 in more detail and provide fourth quarter and full-year 2016 guidance. We'll then take your questions after our prepared remarks. Now I'd like to turn the call over to Sensata's President and CEO, Martha Sullivan.

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

Thank you, Joshua, and thank you all for joining us this morning. I would like to start by highlighting our financial performance for the quarter on slide 4.

Sensata has delivered strong margin expansion in organic EPS growth in the third quarter despite facing challenging markets. We reported quarterly revenues of $789.8 million, which represented growth of 8.6% year over year. And was at the midpoint of the guidance we provided for the third quarter.

We generated organic revenue growth of 1.7% in the third quarter of 2016. With both our performance sensing and sensing solutions businesses generating low, single-digit organic revenue growth. After a 5% organic revenue decline in the first half of 2016, I am pleased that sensing solutions resumed organic revenue growth this quarter.

We continue to deliver on our promise of expanding margins and growing our earnings per share. Our adjusted earnings per share was $0.74 in Q3 2016, which was above the midpoint of our guidance and 2.8% higher than the third quarter of 2015. Excluding the effects of currency and acquisitions, net of exited businesses, we generated 11% organic earnings per share growth compared to the third quarter of 2015.

Our adjusted net income margins of 16% expanded sequentially by 100 basis points compared to the second quarter of 2016. This improvement reflects net productivity gains in our base business and acquisition synergies.

Another key highlight of the quarter is that we are rapidly paying down our debt due to our strong free cash flow. Earlier this year, we committed to getting Sensata's net leverage ratio to between 3.7 and 3.9 times by the end of 2016. I am pleased to report that we further reduced our net leverage ratio and are on track to achieve this target for the full year.

I would note that through the first nine months of 2016, we have consistently executed on meeting our operational targets as well as our investors' expectations. Despite top line headwinds from weaker markets, our organic earnings growth and cash flow performance demonstrate that we are executing to our guidance.

Finally, I want to stress that Sensata has a sustainable, multi-year path to expand our adjusted net income margins. This margin improvement is primarily driven by Sensata's robust operating model. This model is based on driving continuous operating improvements, capturing efficiencies and cost reductions, and leveraging the model to successfully integrate and increase the margin profile of acquisitions. Over time, we believe we will achieve our long-term target of 20% to 23% adjusted net income margins.

Slide 5 shows how we are delivering on our commitment to improve our margins. Since the first quarter of this year, we have improved our adjusted net income margins by 180 basis points, or 210 basis points excluding currency. Our higher ANI margins have come primarily from cost synergies that we have achieved from integrating acquisitions, as well as net productivity improvements in our core business, as a result of best cost sourcing and production efficiencies.

As a part of our integration process, we continue to streamline our global footprint. During the quarter, we made the difficult decision to close our production facility in Minden, Germany, by second half of 2017. This is one of the sites that we acquired through our CST acquisition. We are also on track to close our Springfield, Tennessee plant in the first half of next year, which we have previously announced.

The key message I would leave with you is that we are steadily delivering the margin improvement that we committed to earlier this year. Long-term sustained margin improvement will continue to be a key part of Sensata's performance over the next few years. I illustrate this on slide 6, where I show Sensata's reported and core adjusted net income margins since 2013. There are a couple of key takeaways on this slide.

First, you can see how our adjusted net income margins, shown in blue, are diluted as a result of the DeltaTech, Schrader and CST acquisitions that we completed, and are shown below the chart. A key part of our strategy centers around acquiring companies where we can extend our product reach, globally expand into new markets, and create cost synergies by combining manufacturing, supply chains, and back office functions.

We rarely find acquisition targets that operate at the same high margin levels as Sensata. As a result, acquisitions initially reduce our margins due to the lower profitability, upfront integration investment and interest burden. And you can clearly see this effect on the slide.

Although our reported ANI margins are diluted in the short term from acquisitions, margins grow to the target range over time as we complete integration activities, resulting in strong returns and value creation for our shareholders. In the process, we create scale and increased operating efficiencies in our assets. Additionally, we use our significant free cash flow to repay the debt incurred to finance acquisitions.

The second key takeaway on this slide is that our core adjusted net income margins, which exclude the acquisition effects, have grown to north of 20% over the past few years. In Q3 2016, our core ANI margins were 20.8%, 80 basis points above the low end of our long-term target. This is important, because it shows that our margin expansion opportunity is highly achievable and demonstrates our proven capability to elevate the profitability of acquired businesses to the level where Sensata's core business operates today. As we achieve cost and revenue synergies, and as integration expenses wind down, we have a clear path to generating ANI margins of 20% or more.

While improving our margins remains an important part of value creation at Sensata, I also want to stress that we continue to invest and win important orders that will drive future revenue growth opportunities, which I show on slide 7. Many of Sensata's businesses are tied to the global trends of improving energy efficiency and helping to create a cleaner environment. A good example of where this trend is playing out is in our performance sensing business, where we have developed a sensor for customer's gas direct injection applications.

Gas direct injection or GDI is a fast growing application where Sensata has established an expanding leadership position and is already serving nine major global automotive OEM manufacturers. The reason for this success is that Sensata's sensors provide distinct technical advantages, like vibration resistance and accuracy that allow the OEM a more robust, reliable, and precise gas direct injection system. The enablement of the GDI system helps OEMs drive significant fuel efficiency savings. During the quarter, we secured two important GDI wins against key competitors, totaling approximately $10 million per year. These types of wins will help us drive revenue growth in the future.

On our fourth quarter earnings call, I talked about how we are increasing our sensor content in vehicle electrification. We have been investing in this area to help fuel our long-term growth. In the third quarter, we closed a large order with one of the leading electric vehicle manufacturers. Sensata developed a dual function sensor that addressed the complex requirements of our customer's highly efficient and innovative thermal management system.

We won this business because our sensors provide industry-leading accuracy that enabled the manufacturer to achieve their demanding targets for efficiency. We expect to see our first revenues from this transaction sometime within the next two years. This is a great example of how Sensata can benefit from the growth in vehicle electrification.

Over the past two years, we have been investing to extend our leadership position in tire pressure sensing in China. A key hurdle to achieving this growth is the approval of new TPMS legislation that would mandate the use of tire pressure systems in new passenger cars. During the third quarter, the China Automotive Technology and Research Center, or CATARC for short, finalized a mandate that provided specific details on what companies would need to do in order to comply with tire pressure regulation.

This mandate has been in process since 2010, and its approval represents an important milestone towards passing TPMS legislation in China. CATARC recommends that China OEMs start to comply with TPMS in 2019, and we are starting to see an uptick in sales activity, particularly with multinational OEMs. This would help drive revenue growth beginning in 2019.

We have a lot of attractive growth opportunities in the aerospace market, especially after the CST acquisition doubled the size of our aerospace business. Major customers have now made Sensata a strategic supplier, and our product portfolio, along with our global footprint and product quality, have led to a number of new wins that will drive revenue growth over the next few years.

Finally, one of the more exciting investments we are making for growth is our partnership with Quanergy to develop LiDAR sensors for the autonomous driving market. At this point, we are only seven months into the partnership, but we have been validating strong customer desire for solid state LiDAR sensors, given the attractive market for autonomous vehicles. We continue to make technical progress and are collaborating closely with Quanergy. We believe that this market has great potential and that we have a fundamental advantage with our approach to solid state LiDAR sensors. We will provide you additional updates next year.

An update on Sensata's market and business trends are summarized on slide 8. For the full-year 2016, we aren't seeing any significant major changes to Sensata's markets. But we are seeing pockets of weaker revenue performance as we enter the fourth quarter.

For automotive, which is our largest market, we expect that our core auto business, excluding TPMS, will grow 5% organically for the full-year 2016. This growth is stronger than the market, as a result of strong contact growth, particularly in China, where our business has been robust. That being said, as we look ahead to the fourth quarter, we believe we will see a slight downtick in our North American auto business, due to end-of-year inventory corrections. Additionally, our European TPMS aftermarket business has also been soft due to lower demand for winter wheel tires. This will also have a modest negative impact on our Q4 revenues.

We have continued to outgrow the market in our heavy vehicle and off-road business. Through the first nine months of the year, we generated a 3.4% organic revenue decline, compared to the same period in 2015. This performance was clearly better than the overall HVOR market, due to our content growth. The Class 8 North American truck market has declined throughout the year and was down approximately 27% at the end of the third quarter. We believe we will continue to perform better than the market in HVOR despite continued weakness entering the fourth quarter.

Sensing solutions organic revenue growth has sequentially improved each quarter of 2016, improving to a decline -- from a decline of 7% in the first quarter to 2% organic revenue growth in the third quarter of 2016. For the full-year 2016, sensing solutions will largely be on track with our expectations.

However, entering the fourth quarter, we are concerned about high inventory levels of compressors and motors, particularly in China, and we expect our revenues will slightly lower than previously expected in the fourth quarter. We expect foreign exchange rates in the fourth quarter of 2016 to be roughly in line with our previous expectations. Revenues will be lowered by approximately 1% to 2%, and EPS will be lowered by approximately $0.05 in the fourth quarter of 2016 due to currency.

So, to summarize my comments on slide 9, despite challenging market conditions, we are on track to deliver our adjusted net income and earnings per share guidance for full-year 2016. We are making good progress in expanding our adjusted net income margins and generating organic EPS growth. We expect this trend to continue in 2017 and beyond.

We are driving continuous operating improvements, capturing efficiencies and cost reductions and leveraging our operating model to successfully integrate and increase the margin profile of acquisitions. Finally, we are delivering on our promise to pay down debt and improve our net leverage ratio, and we will continue to strengthen our balance sheet over the next few quarters.

I would now like to turn the call over to Paul to review our third-quarter results in more detail and to provide financial guidance for the fourth quarter and full-year 2016. Paul.

Paul Vasington - *Sensata Technologies Holding N.V. - CFO*

Thank you, Martha. Highlights for the third quarter as shown on slide 10 include, revenue of $789.8 million in the quarter. An increase of 8.6% from the third quarter of 2015.

Of this growth, the acquisition of CST less exited business contributed 8.6%, organic revenue growth was 1.7%. Changes in foreign currency exchange rates, primarily to Europe, represented a net revenue headwind of 1.7%. Those segments generated positive organic revenue growth in Q3 of 2016.

Performance sensing continue to deliver above-market growth, reporting 1.5% organic revenue growth in the quarter. This was a result of solid content growth from our automotive and HVOR businesses. Sensing solutions generate organic revenue growth of 2.4% on stable demand and either comparison to the prior-year quarter. From a geographic perspective, Asia drove most of the organic revenue growth, with very high growth rates from China due in part to an easier year-over-year comparison.

Adjusted net income was $126.3 million, or $0.74 per share and better than the mid-point of our guidance.

When compared to the prior year, adjusted net income and adjusted earnings per share were up 2.4% and 2.8%, respectively. Adjusted net income margin of 16% in the third quarter was down 1% year over year. But up 100 basis points sequentially from Q2 2016.

Martha talked about our core ANI margins earlier in the call. If we exclude the impact of foreign currency and the effects of acquisitions and exited businesses completed in the last 12 months, which is primarily CST, our organic adjusted net income margin was 18.6% in the third quarter of 2016, up 150 basis points over the prior year. This is primarily due to higher operating efficiencies and net productivity gains, as well as lower interest expense.

Research, development and engineering expenses were $67 million in the third quarter, or 8.5% of revenue. Adjusted taxes were 6.1% of adjusted earnings before interest and tax. Integration costs were $3.9 million in the quarter. Restructuring and special charges of $4.2 million added back to our non-GAAP numbers in the third quarter, but primarily related to optimizing our global manufacturing network. Finally, we increased our free cash flow by 11% year over year to approximately $120 million, due primarily to higher adjusted net income and lower capital expenditures.

Now, I'd like to comment on the performance of our two business segments. I will start with performance sensing on slide 11.

Our performance sensing business reported revenues of $584.7 million for the third quarter of 2016. Representing growth of 1.4%, compared to the third quarter of 2015. Excluding the impact of foreign currency and acquisitions less exited businesses, performance sensing generated 1.5% organic revenue growth in the quarter, which was primarily driven by content growth, as well as sharp recovery in our automotive business in China.

Our automotive businesses had mixed results during the quarter, however in total, we're largely in line with our overall expectation. Heavy vehicle and off-road generated an organic revenue decline of 3.5% in the quarter and continued end market weakness in North America on-road truck, as well as in global construction [in] agriculture. Somewhat offset by content growth. Overall, the ACR revenue decline was better than expected.

Performance sensing profit from operations was $155.2 million or 26.6% of revenue. Up 40 basis points from the year-ago quarter. Excluding the impact of foreign currency and CST, profit from operations would have been 27.6%, a 140 basis-point improvement from the prior year due to improved operating efficiencies and net productivity gains in cost reduction.

Next, I will turn to our sensing solutions performance on slide 12. Sensing solutions reported revenues of $205.1 million in the third quarter of 2016, up 36% from the year-ago quarter, due primarily to the impact of acquired revenue from CST.

Sensing solutions reported organic revenue growth of 2.4%, which is a nice rebound from the 5% organic revenue decline as the second posted in the first half of 2016. From a geographic perspective, this organic growth was driven by Asia and particularly China. Sensing solutions end markets remain broadly weak. However, year-over-year comparisons are easier, given the even more challenging markets last year.

Sensing solutions profit from operations was $67.3 million, an increase of 35% from the same quarter last year, due to effects from CST and productivity gains. As a percentage of revenue, sensing solutions profit from operations was down 20 basis points to 32.8%.

Excluding the impact of foreign currency and CST, profit from operations would have been 33.8%, an 80 basis-point improvement from the prior year, due to operational efficiencies in cost reduction. Corporate and other costs not included in segment [op] income were $48.3 million in the third quarter.

A key area of focus for Sensata has been to reduce our debt and net leverage. Slide 13 shows our debt reduction in net leverage ratios since we completed the CST acquisition in the fourth quarter of 2016. On a yearly basis, we have paid down approximately $300 million in debt while improving our net leverage ratio from 4.6% to 4.0%.

This is considerable progress in only three quarters, and we are on track to deliver net leverage of 3.8% by the end of 2016. Which is within the guidance we provided earlier this year. Also, assuming we don't close any new acquisitions, we would expect our net leverage to be about 3 times by the end of 2017.

Now, let me turn to our financial outlook for the fourth quarter on slide 14. Before we begin, I want to point out that Sensata acquired CST on December 1, 2015. And our standard practice, is to include results in our organic performance after 12 months. As a result, we will have one month of CST results reflected in our organic revenue and earnings performance for the quarter and the full fiscal year.

In the fourth quarter of 2015, CST generated a $0.06 loss, primarily related to integration charges and interest expense. As a result, there was a significant swing in CST's profitability and a corresponding impact on our adjusted net income and organic EPS growth in the fourth quarter of 2016. For clarity purposes, we have shown our guidance with CST results included from December 1 onwards, and [with an] excluded for the entire quarter and fiscal year to make it as easy as possible to analyze our guidance.

As Martha mentioned earlier, we are adjusting our revenue outlook due to three specific factors. One, higher year-end inventories in North American auto market. Two, European TPMS aftermarket due to lower winter wheel tire demand. And three, higher compressor and motor inventories in China, which will affect our sensing solutions business.

We are factoring this into our fourth-quarter guidance, and as a result, we expect to generate revenues between $765 million and $805 million. The mid-point of this guidance represents revenue growth of approximately 8%, and organic revenue growth of approximately 4% compared to the fourth quarter of 2015. Our current [flow] rate stands at approximately 82% of the mid-point of this guidance.

Despite the modest change in revenue, we will not change our annual earnings guidance, as we expect to report between $123 million and $133 million of adjusted net income, [and]adjusted earnings per share between $0.71 and $0.77, based on our fully-diluted share count of 171.6 million. The mid-point of our EPS guidance represents approximately 12% reported earnings growth, and 21% organic earnings growth. We expect foreign exchange rates will lower our revenue by approximately 2% in the fourth quarter compared to 2015, and lower our adjusted EPS by approximately $0.05. The mid-point of our fourth-quarter 2016 guidance assumes that we achieve an adjusted net income margin of 16.3%, slightly better than we reported this quarter.

Our financial guidance for the full-year 2016 is shown on slide 15. Our revenue guidance for Q4 implies that we will be approximately $10 million lower than the mid-point of our previous guidance for the full-year 2016. We are maintaining our full-year earnings per share guidance, but narrowing the range.

We expect to report revenues between $3.18 billion and $3.22 billion. The mid-point of this guidance resumes reported revenue growth of 7% to 8%, and organic revenue growth of 1% to 2%. We expect to generate adjusted net income of between $487 million and $497 million, with adjusted EPS of between $2.84 and $2.90. The mid-point of our adjusted EPS guidance represents approximately 4% reported earnings growth, and approximately 11.5% organic earnings growth. We expect the impact of foreign exchange rates to reduce our adjusted earnings per share by $0.19 to $0.20 for the full year of 2016.

I will conclude my remarks by summarizing Sensata's investment summary on slide 16. Sensata's goal is to win in sensing. The sensing market is attractive and growing, and we've been a leader in this space for over 25 years.

We expect to generate strong returns from the acquisitions we have completed and are diversifying our end-market exposure. Future returns from recently-completed M&A transactions are a pillar of our growth strategy and one of the ways we differentiate ourselves. We generate attractive long-term revenue and earnings expansion, and we are poised to sustain this performance in the future.

Finally, Sensata is a high margin, high-cash generation business. Our margins are borne out of long-cycle revenue, highly differentiated products, and extremely cost-effective manufacturing operations. Strong margins coupled with a low cash tax rate drives strong free cash flow to allow Management to generate strong returns for investors. Now, I'd like to turn the call back over to Joshua.

Joshua Young - *Sensata Technologies Holding N.V. - VP of IR*

Thank you very much. Beth, please assemble the Q&A roster.

QUESTIONS AND ANSWERS

Operator

Thank you, Mr. Young.

(Operator Instructions)

The first question comes from the line of Amit Daryanani, RBC Capital Markets, your line is open.

Amit Daryanani - *RBC Capital Markets - Analyst*

Thanks, good morning, guys. Two questions from me.

One, could you walk through the time and levers you have to get your adjusted A&I back towards a 20%, 23% target for the total Company? Is the two site closures that you talked about today enough to get there? And what sort of timeline should we expect to achieve those targets?

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

Amit, the second half of that about the cycles. Can you repeat that?

Amit Daryanani - *RBC Capital Markets - Analyst*

Yes, I was just trying to understand, when do you get the adjusted net income margin target that you have of 20% to 23% for the entire Company? And do the two site closures, one in Germany and one in Tennessee that you talked about, is that enough to get the total Company within the target or does there need to be more restructuring to get there?

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

Okay, there are a number of things still ahead of us in terms of improving the profitability of our acquired businesses. And so those two consolidations are certainly important steps in the direction, but by no means are we complete. We generally will talk, Amit, about a three-year cycle to complete integration; and in the case of Schrader, we actually extended that to four years, because we did little to restructure in the first year of that acquisition. You might recall it was going through a big ramp in Europe. So, if you look at where we are, that would take us out into the 2019 time horizon on the acquisitions.

The other thing to be mindful of is, there's a variable on all this, and that is what will our overall interest rate expense be? That would be one more swing factor. And that is subject to a lot of things that we would want to be thinking through as we look at ways to create value for our shareholders.

Amit Daryanani - *RBC Capital Markets - Analyst*

Got it. Follow-up, a fair amount of discussion what auto production numbers look like as we go into 2017. Would love to get whatever initial assessment you have across the GOs, and how you think auto production shapes up for the next year?

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

I will tell you, with one exception, and that's the exception being China, we're not seeing any sort of significant disruptions in the landscape in auto. We are not expecting much help from mature end-market production as we move into 2017. What becomes really important for us is to get through the quarter and look at what actual backlog is doing. In the case of China, we're seeing a very strong second half, not surprising given the incentives that are in place there. And we think growth will slow in China, but still be really attractive. If you look at underlying secular demand and the insulation rate of vehicles per driver population, it's still very attractive in China, the tax movement notwithstanding.

So, we think end market growth slows there. We continue to grow way above end market in China and expect to continue to do that as we go forward.

Amit Daryanani - *RBC Capital Markets - Analyst*

Perfect, thank you.

Operator

Your next question comes from the line of Wamsi Mohan, Bank of America. Your line is open.

Wamsi Mohan - *BofA Merrill Lynch - Analyst*

Yes, thank you, good morning.

So Martha, clearly, HVOR is still a headwind, so is TPMS; North American auto seems to be at a high inventory level. So, performance sensing is just not growing at the same faster pace that we were hoping for. In this environment, how are you thinking about the need to maybe accelerate some of the initiatives around integration activities? So potentially, not being $0.20 incremental in each of the next few years, but being able to pull forward some of that? Do you have a plan to do that in case the demand environment continues to be relatively weak? And I will follow up.

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

Yes, you know, so the relatively weak part probably wouldn't drive a major change in our overall cadence on integration. We have continued to pull forward some of that and you can see that on the steady pace of margin improvement across the business, and including in the base acquisitions. In the event that we saw something quite disruptive, we experienced a demand contraction, that would have us lowering our utilization rates across our asset base and would allow for some significant acceleration. And we have been able to execute in that fashion in past cycles.

Wamsi Mohan - *BofA Merrill Lynch - Analyst*

Okay, thanks, Martha.

As a followup, when you look at the European auto revenues, which were weaker both on quarter-on-quarter and year-on-year basis, can you talk about how much of that may be on a quarter-on-quarter basis with seasonality versus the weaker aftermarket that you alluded to on TPMS, versus anything potentially Brexit related? And on China TPMS it sounded like that was going to contribute to revenue growth in 2019. I think in the past you have said some of the OEMs might adopt this earlier. Are you still expecting an earlier adoption despite the official timing? Thanks.

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

Just to answer the second question first, we are seeing some earlier adoption on that front. Still small, but we're actually, we have a run rate on TPMS now, and we expect to have one that is stronger next year. On the European front, the winter wheel effect is fairly significant in the quarter, because it is a very seasonal development for us. So, I'd say that's a fairly significant part of the overall. The other thing that we watch carefully: we've talked in the past about headwinds relative to diesel installation. We think that those are slow; we are expecting about a 5% contraction in the take rates over the next three to four years. And that's about what we are experiencing as well that you might not see in the production rates.

Wamsi Mohan - *BofA Merrill Lynch - Analyst*

Thanks, Martha.

Operator

Your next question comes from the line of Shawn Harrison, Longbow Research. Your line is open.

Shawn Harrison - *Longbow Research - Analyst*

Morning, everyone. Two-parter.

First, on just the North American auto situation in terms of the excess inventory. Do you believe that will be cleared up exiting the calendar year? And second, on the sensing solutions business, particularly the excess inventory in China. It's been a theme for probably the better part of two-plus years now, sometimes worse than we're seeing now, sometimes a little bit better. But is there a thinking that you begin to underproduce the market just to secure yourself from having to talk about higher levels of excess inventory and talking down revenues in future quarters related to this business?

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

Sure, on the North America front, we're largely calling the quarter based on backlog. And so, as we roll into a quarter, we have got about 82% of it secured in actual order rates. And so the reconciliation that we do when we look at that order pattern versus where we think production is, it really is how we predict some takeout on inventories. We would expect those to be corrected before we move into next year.

On the sensing solutions piece, not a lot of options to underproduce. And so, we are in the position of being sole supplier to many of our customers. We work closely with them to try to understand what their component inventory level is. The one thing that is somewhat out of our control is how much of their equipment they inventory. And so, that will have us in times overperforming and underperforming the market, given the overall compressor and motor buildup. That's what we are expecting to see in the fourth quarter.

Shawn Harrison - *Longbow Research - Analyst*

Okay. And then just one brief followup, if I may.

If you were to rank the impacts on revenue for the fourth quarter in terms of North America, TPMS in Europe, or other factors? If you could do that, that would be of great help, Martha.

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

You know, fairly balanced, to be honest. I would say particularly for those first two, quite balanced. Probably a little smaller impact, just given the size of the business on the inventory in China for sensing solutions.

Shawn Harrison - *Longbow Research - Analyst*

Very helpful, thank you.

Paul Vasington - *Sensata Technologies Holding N.V. - CFO*

I would like to add that sensing solutions, if you think about the whole year, the full year of 2016, we're in line with where we thought we were going to be. Actually might be a little better. So, I think that business has performed pretty well, despite this little hiccup in Q4.

Shawn Harrison - *Longbow Research - Analyst*

Thank you.

Operator

Your next question comes from the line of Christopher Glynn, Oppenheimer. Your line is open.

Christopher Glynn - *Oppenheimer & Co. - Analyst*

Thanks, good morning.

Martha, thanks for putting the stake in, so to speak, with the 2019 time frame for the integrations and the A&I targets. Is sort of ratable progress the way to think about that?

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

No, I would be careful not to assume that. So you can see, for example, some of the things that are driving that improvement. If you just think through the mechanics of consolidating on the manufacturing level, that involves a process of some significant integration spending. Actually building inventory in the high-cost location, going through an approval and validation process into the low-cost location. And then drawing down that inventory, which makes it really unlikely that, that develops in a linear way. So, I would be careful on that.

And then I would just say, again, one of the factors in this is in what ends up happening with our overall interest expense. As we get to 2019, we would expect to see good operating performance in the acquired business, particularly as we exit that year. It's going to be a question of where we stand on our overall debt burden at that point.

Christopher Glynn - *Oppenheimer & Co. - Analyst*

Okay. Are you starting to suggest that you're seeing the makings of higher-cost refinancing?

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

No. Not at all. Not at all. We are absolutely not.

Christopher Glynn - *Oppenheimer & Co. - Analyst*

Okay. And then on FX, I know they are going to change the rates the next few months. We don't know which way. But as things stand right now, what are we steering towards for range of FX impact for 2017? Because that was quite a big factor this year that you had to deal with.

Paul Vasington - *Sensata Technologies Holding N.V. - CFO*

So, next year, in 2017, it is still too early to know for sure, as we continue to hedge for the rest of the year where rates are moving.

Christopher Glynn - *Oppenheimer & Co. - Analyst*

Stipulating.

Paul Vasington - *Sensata Technologies Holding N.V. - CFO*

Year over year, foreign exchange will probably be a couple of cents negative. So a couple cents down. Or negative impact to earnings. So, we have $0.19 to $0.20 down this year. So, next year will be a couple pennies.

Christopher Glynn - *Oppenheimer & Co. - Analyst*

Thanks, Paul.

Operator

(Operator Instructions)

Your next question comes from the line of Craig Hettenbach, Morgan Stanley. Your line is open.

Craig Hettenbach - *Morgan Stanley - Analyst*

Yes, thanks.

Appreciate the color on North America and inventory, what you're expecting to year end. Could you extend that into China and Europe? Certainly, China, the growth is very strong, but as you see OEMs and suppliers manage inventory into the market that we're seeing right now?

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

The China phenomenon is not really where we are on inventory. There is very strong demand right now. I think everyone close to that issue is recognizing there are some incentives that are driving consumer behavior. And I think the swing point is going to be what happens to those incentives as we move through 2017. We're not seeing significant inventory build in year up. Not really a factor.

Craig Hettenbach - *Morgan Stanley - Analyst*

Got it, thanks.

And then, if you could talk to just the strong free cash flow, you levering the balance sheet versus M&A. Clearly, you guys have been very active in recent years in the M&A front. As you look forward, what the priorities are in terms of balance sheet versus looking for growth opportunities?

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

Yes, I think looking forward, we're going to be at a normalized rate by the time we get to the end of 2017. And so, we'll go back to what is the best way for us to create value for shareholders? Our M&A pipeline is active. We tend to execute proprietary deals. The cadence and timing of that will come naturally as those projects advance. We continue to think it's a great way for us to create value for shareholders. You can see it in the earnings growth that we're delivering in the businesses that we have acquired. But at the end of the day, we'll look at using a repurchase decision as the benchmark for whether or not that is the right way to create value for our shareholders.

Craig Hettenbach - *Morgan Stanley - Analyst*

Got it, thanks.

Operator

Your next question comes from the line of Matt Sheerin, Stifel. Your line is open.

Matt Sheerin - *Stifel Nicolaus - Analyst*

Yes, thanks, and good morning.

So, question regarding the HVOR market, where sounds like fundamentals are a little bit better than expected, despite continued end market weakness. You talked about content growth there. Is that from new products or additional regulatory mandates? And do you think you can begin actually growing that business into next year, even as North America continues to be fairly weak?

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

So, let's recognize the end market is absolutely not incrementally better. It's actually gotten -- Yes, anticipated some of that. And so, to be declining 3.5% on markets that are down very strong double digits, I think is a testimony to the content growth.

We do expect continued content growth in that business. It's driven by a few things. One is greenhouse gas regulations that are developing. We're also seeing lots of interest in tire pressure sensing in the heavy vehicle market. You think about what that does for fuel economy gains for fleet users; it's an exciting opportunity.

We see lots of interest in improving the overall efficiency of off-road equipment. So when we look at our operator sensing controls, that's an opportunity for us as well. So, despite the end market demand weakness, it's a pretty exciting market for Sensata, when we look at the content opportunity.

Matt Sheerin - *Stifel Nicolaus - Analyst*

Okay, thanks.

And just as a followup, regarding the Quanergy investment and partnership there, was there anything you can tell us about when we would expect any kind of pilot programs of products? Outside of your investment with them, are you actually investing any resources internally in terms of production or R&D outside of that partnership?

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

Well, yes, we have a number of investments and it's a pretty broad pipeline on the R&D side, I think, to speak specifically to timing on solid state LIDAR sensing. Our expectation has not changed a lot. We think that, that is still in the 2020 to 2023 timeline, where we get to, I think, real momentum building in revenue and that is the important thing. So, plenty of pilots and demos ahead of that. But I think what is going to be important to investors is actually securing material contracts, and that's the time horizon.

Matt Sheerin - *Stifel Nicolaus - Analyst*

Okay, thank you.

Operator

Your next question comes from the line of Mark Delaney, Goldman Sachs. Your line is open.

Mark Delaney - *Goldman Sachs - Analyst*

Yes, good morning, and thanks very much for taking the questions.

The first question is on the two site closures you announced. Can you quantify what the annual cost savings would be for each of the two site closures that you announced? And then how long you think it will take before you get to those full run-rate savings?

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

I really can't quantify that off the top of my head at this point. If you look at the accretion that we've predicted for the acquisition, it's an important step. These are important steps, but certainly not the only steps as we look forward.

Mark Delaney - *Goldman Sachs - Analyst*

Okay, understood. And then a followup question on the fill rate. I think the comment was 82% fill rate based on your fourth-quarter guidance this year. I think last year, the assumption was an 86% fill rate. If that's right, can you help us understand the reason for the change in terms of the guidance versus the fill rate?

Paul Vasington - *Sensata Technologies Holding N.V. - CFO*

The fill rate, if you look back to what we saw in the last quarter, we're about the same level at this time. So, I think the fill in the order flow is fairly consistent with what we have seen over the course of the year.

Mark Delaney - *Goldman Sachs - Analyst*

Thanks very much.

Operator

Your next question comes from the line of William Stein, SunTrust. Your line is open.

William Stein - *SunTrust Robinson Humphrey - Analyst*

Thanks for taking my question and good morning.

Martha or Paul, can you remind us how much incremental EPS we should think about as still coming from the acquisitions that have been closed? And in particular, what that transition would be expected in 2017 versus 2016? So, for example, if we got no meaningful organic growth in the core business, what the EPS growth should look like?

Paul Vasington - *Sensata Technologies Holding N.V. - CFO*

I would first start with that we are seeing quite a bit of growth in the core business, and you can see it in the information we have been presenting that. We are driving significant margin expansion and productivity gains in the core business. The integrations have been going well. We have been consolidating manufacturing and the back offices. What hasn't been going so great, and it's obvious in the end markets that those -- serving our [weak], the incremental EPS that we originally expected from those acquisitions was going to be less. But the EPS benefit from the core business, given all the strengths and all the operational improvements we made is going to be more. Which is why we are allowed to hold and stay on the guidance for the year.

As we continue to go next year, we're going to continue to integrate and continue to improve initiatives, which will continue to be a tailwind for earnings growth in 2017 and beyond.

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

I think another way to think about that is, we've talked about fewer headwinds as we go from 2016 to 2017, relative to currency. We're coming through a year where we spent fairly heavily on integration. We'll spend again next year, and you can see the overall earnings performance of Sensata. So, all of what we just described is within our control, and we don't see things on the horizon that are big discontinuities to our overall ability to impact earnings, even with lackluster end market.

Operator

Your next question comes from the line of Jeremy Ketron, CLSA. Your line is open.

Jeremy Ketron - *CLSA - Analyst*

Thank you, good morning.

I wanted to ask you about your pricing and material cost dynamics in recent quarters and how you think about it going into next year? Thank you.

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

Yes, our pricing has been in line with expectations and we don't see, again, a major transition on that front. We have a couple phenomena to think about in pricing. Some are the way everybody thinks about it, where we actually will deliver price downs in a multi-year contract. Another element, though, is we often will introduce next generation products that have a lower price point, but higher margin performance. So that is part of the overall price movement that you'll see as well. And we're in a period of that right now, which probably extends into 2017 as well. Overall, we talk about a 2% down framework across Sensata.

Jeremy Ketron - *CLSA - Analyst*

What about the material cost side of things?

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

The material cost side of things. You know, commodities are not a big portion of our overall material spend.

Paul Vasington - *Sensata Technologies Holding N.V. - CFO*

I think to the question, we continue to drive material costs out of our products, which has allowed us to continue to have net productivity gains. Greater cost reduction to offset the annual price down, continue to expand our gross margins. It's a core part of our business and something we have a rich history of doing.

Jeremy Ketron - *CLSA - Analyst*

Thanks; and Paul, on the free cash flow outlook for the year. Any change here? Looks like you are trending slightly above target for the full year, and how do we think about some of the major moving pieces for free cash flow in 2017?

Paul Vasington - *Sensata Technologies Holding N.V. - CFO*

Two key things to take away: the cash flow looks like it's going to be in the upper part of the range. So, we were $350 million, $400 million; it's looking more like $375 million to $400 million is where we think we'll land. What's driving that is the strong income, as well as lower CapEx, so we continue to look for ways to reduce the capital intensity of the business. Get more output of existing assets, and so we've been able to continue to support demand with less incremental CapEx this year.

Operator

Your next question comes from the line of Samik Chatterji, JP Morgan. Your line is open.

Samik Chatterji - *JPMorgan - Analyst*

Hi, good morning.

I wanted to go back to the TPMS opportunities in China. I know with the share of business, you have high market share of the market in North America and Europe. I think you bucketed that as 50% share in the past. With demand getting past here in Q3, is a 50% market share still a fair assumption for making sure things can play out? Or does the mandate change any expectations as to what share you can have of that market in TPMS?

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

Yes, you're a little bit high on our share, but it is quite strong, as you point out. It's between 40% to 45% on a worldwide basis. We expect to do that well in China, which is why we moved very quickly post the acquisition to put manufacturing there and to begin to engage with customers. So, we have been achieving design-in opportunities right from the get go. And we're really pleased by the momentum we're having there.

Samik Chatterji - *JPMorgan - Analyst*

Great, just one followup.

Looking on longer-term in terms of what you are seeing from hardware makers in relation to power strain strategies, we are hearing about concerns adding diesel mix in Europe, and that has been a concern. But, are you, when you mention sensor (inaudible) electrification of the power creating strategies from (inaudible) looking more inclined toward hybrids? Or are they looking at more like (inaudible) vehicles? And if you can remind us of what your content opportunity on each of those are separately?

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

Yes, so you know, it's a time that of a really fluid power train strategy across the board. So, we see heavy spending on getting conventional combustion engines to very high levels of efficiency. And everybody has an electrification strategy to go alongside that. So, what we see is, we do expect to see some decline of diesels in Europe. I think that's tend to have been overstated, if you go back to the dieselgate eruption. So, it's above a 5% share lots in Europe on diesel take rate over time. And that has a gap on our sensor content right now. As we achieve things like design wins and gas direct injection, we're closing that gap. When we get to the three- to four-year time horizon, we don't think there's a big difference between Sensata content on gas versus diesel.

On the electrification front, we do better overall on sensor content with a hybridized vehicle, or as soon as customers move to any level of electrification. We had conventionally not done well on full plug-in electrics, but we are closing that gap quickly. We talked about a key win we saw this quarter. We are playing across the landscape on that. On all of those avenues, and it's driving our content opportunity as we look ahead.

Operator

Your next question comes from the line of Jim Suva, Citi. Your line is open.

Jim Suva - *Citigroup - Analyst*

Thank you. It's Jim Suva. A strategy question, probably for Martha, and then a clarification for Paul.

Martha, on the strategy, it sounds like you're making good progress at de-leveraging the balance sheet. As you go about that strategy, the timeline around this time next year, the second half of next year, where then your ratios are more comfortable, were then the M&A probability increases? And then should we just look at this as a circular wheel, for example, you make acquisitions, you lever up the balance sheet, and use the cash flow to pay it down, and integrate it and get inner synergies -- is that the way to think about the time line?

For Paul, the clarification questions are, for the FX impact, you saved a few pennies next year. Can you remind us what rates you're referring to, maybe back forward versus spot versus current for the rates? And then on the tax rate, are we looking at still a very low tax rate of, say, 7%, say, through 2025? I believe if I remember right, it was from your IPO asset markup days and the amortization of the step-up costs. Thank you very much.

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

On the leverage question, you're right. As we get to the second half of next year, we get back to what's a more natural level for Sensata. And the level we are quite comfortable with. Given our cash flow, we are comfortable with where we are operating today.

As it relates to probability of M&A, I think the thing to think about is that there are a number of factors that impact the probability of M&A, and right now we have a fairly high hurdle rate on M&A, given where our leverage is. We would probably reduce that somewhat, our internal hurdle rate, as our debt ratio improves. But we've really got to make sure that what we are acquiring aligns closely to our strategy and that we can get it at the right price, and that we can bring it to Sensata's margins in a reasonable time horizon. Those are the other things that can have an impact on what actually gets done over time.

I'll turn it over to Paul to address the other two.

Paul Vasington - *Sensata Technologies Holding N.V. - CFO*

On foreign exchange, you have to go back a bit when we first started to see the maps of decline of the euro. In that 2015 time period, we were really well-hedged. We have been hedging out about a year and a half to two years. We were protected in 2015, because our hedges held up the value of our euro rates as a company. Even though the spot price was dropping dramatically. In 2016, many of those hedges had rolled off, and as we continue to hedge into 2016, we're hedging at lower rates. What's happening now is, the spot rate and average hedge rate, all-in rate, they're coming closer together. And all the bad news is really happening in 2016. As we get into 2017, our hedge rates are going to be closer to what you are seeing the euro trade today.

The other big currency that is helping us, quite frankly, is the peso; it's the opposite story. So, as we look into 2017, our average hedge rates and our spot rates are coming closer together. That's the key takeaway.

As it relates to tax, this year, we are 5.5% to 6.5%. We'll probably come in around 6% for the full year. Next year, the tax rate will stay in the 6%-ish, 6.5%-ish range for a period of time that will gradually move up as we use tax benefits over time. But I think over the next three to four years, we're going to be in the 6% to 7% range for quite a while.

Operator

Your next question comes from the line of Rich Kwas, Wells Fargo Securities. Your line is open.

Rich Kwas - *Wells Fargo Securities, LLC - Analyst*

Hi, good morning, everyone. Just a couple of follow-ons from me.

On CST, on the transaction, is the expectation that EPS accretion still reaching that $0.23 to $0.26 range by year three, even with the underlying softness in their business right now?

Paul Vasington - *Sensata Technologies Holding N.V. - CFO*

Yes, Rich, I would say that's what we are still targeting, but it does become a little bit more challenging with the softness we are seeing in the end markets. But I would say that the integration activities are going really well. We continue to see opportunity there. So, too early to call that, but certainly we definitely do have some market headwinds that we have got to deal with.

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

On the flip side, as we have seen more cost opportunity in that acquisition, and are executing on that quickly and well, the other thing to think about, because as you reach out in time, what is impacting the top line in CST is some of the familiar things in end markets. So, a significant part of their exposure is in HVOR, and we don't expect that, that is going to be a down market for the next three years.

Rich Kwas - *Wells Fargo Securities, LLC - Analyst*

Okay, understood. And then, Martha, I know it's early, but if you could just help us think about, at least qualitatively, about 2017. You have key end markets that you are levered to, that are either at peak or have already taken a hit. And there's probably likely some more deterioration potential in 2017. Right now, I know, I understand you are probably going through the planning process right now. But as you think about organic growth for 2017, what are the key puts and takes as you see it right now?

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

Yes, look. End markets on 2017, we're all going to do our work. You guys will. We'll do our work. We'll all come to our own conclusion on where that lands. The insight that we have that you don't have is what actually happens in the order of patterns as we move into the year. We think that's an important part in calling the overall year. We're going to take our time to make sure we separate out inventory impacts from actual end market demand. And that's particularly important in China. To just given that we're seeing very strong growth there. It has seen it historically, where we're at the highest levels we have ever seen. Don't think that's completely sustainable, given what is going on with tax incentives. But a big piece of that is content growth, and we want to make sure that, that's on track as we move into next year.

So, the puts and takes are familiar things. What are end markets going to do, and what will happen with the actual launch timing of design ends that we already have secured and are in place, and I think that's what we're going to have to work through.

Rich Kwas - *Wells Fargo Securities, LLC - Analyst*

Okay. Great, thank you.

Operator

Your next question comes from the line of Ambrish Srivastava from BMO. Your line is open.

Ambrish Srivastava - *BMO Capital Markets - Analyst*

Thank you very much.

Martha, lots of details. I just have two quick clarifications. Talking about the US inventory level, we have seen the data Q3, the published data was levels US light inventory, vehicle inventory was up, if I recall correctly, four or five days. So, are you indicating by your comments that you expect further acceleration in that inventory build, and could you quantify it? And then my second clarification: on China, your crystal ball is definitely better than mine. Year over year, what do you expect the unit production to be? And where do you expect it to normalize at? Thank you.

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

I'll hit the China one separately, make sure we are talking about the same thing there. On vehicle inventory, look. At this point, what we're looking at is our actual backlog and who we're shipping to and what it might suggest about their production rate. How that manifests into OEM days of dealer inventory is going to be their choice. We're really not forecasting what happens with vehicle inventory at the end of the year. We're in the time period where our order pattern is the most insightful thing we can use to give you the appropriate guide.

I think when we look at China, for the overall year, we're predicting, just looking at my notes here, we're predicting the overall end production, which is what we monitor, to land at something like double digits for the year. I'm just checking my notes on that. You know, we're seeing something like 30% to 40% growth in the quarter. So that is, that's not something, obviously, that's sustainable. But a big piece of that is overall content growth. So --

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Paul Vasington - *Sensata Technologies Holding N.V. - CFO*

Single digit.

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

I'm sorry.

Paul Vasington - *Sensata Technologies Holding N.V. - CFO*

For market.

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

We're probably more like 8% to 9% on the overall end market in China.

Ambrish Srivastava - *BMO Capital Markets - Analyst*

In Q4; and then your business is up 30%, 40%, right?

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

Yes, that was on the year. And in this quarter, we're up to that 30% to 40% level. We'll probably end at twice the end-production rate.

Ambrish Srivastava - *BMO Capital Markets - Analyst*

And what do you expect it to normalize at, was the second part of the question.

Martha Sullivan - *Sensata Technologies Holding N.V. - President and CEO*

I'm probably not going to give you a useful response to that at this point. The thing I'll tell you is that we did quite a bit of work, this goes back to when we saw the big correction in China last year, to just try to understand what will happen to secular demand on vehicles. And when we did that work, we saw something like a 4%, 3% or 4%, overall production growth over a five-year time horizon. How that translates in any given year, it can be an impact of incentives one year; no incentives the next year. So I think you need to be really careful in thinking that through.

Ambrish Srivastava - *BMO Capital Markets - Analyst*

Thank you for the transparency. Appreciate it.

Operator

I'd like to turn the conference call back to Mr. Young for closing remarks. Mr. Young?

Joshua Young - *Sensata Technologies Holding N.V. - VP of IR*

Thank you, Beth, I would like to thank everyone for joining us this morning. We appreciate your continued interest in Sensata. Sensata will be attending the following investor conferences in the fourth quarter: the RBC Tech Conference on November 9 in New York, and the Credit Suisse Tech Conference in Phoenix, and the Bank of America Smid Cap Conference in Boston. We encourage you to meet with us at these conferences or meet with us at our headquarters in Attleboro. Thank you, and goodbye.

Operator

That concludes the call for today. You may now disconnect.
