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SCSC.OQ - Q3 2026 Scansource Inc Earnings Call

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CORPORATE PARTICIPANTS

Mary Gentry *Scansource Inc - Senior Vice President, Treasurer and Investor Relations*

Michael Baur *Scansource Inc - Chairman of the Board, Chief Executive Officer*

Steve Jones *Scansource Inc - Senior Executive Vice President, Chief Financial Officer*

CONFERENCE CALL PARTICIPANTS

Keith Housum *Northcoast Research - Research Analyst*

Gregory Burns *Sidoti & Company LLC - Analyst*

Logan Katzman *Raymond James - Analyst*

PRESENTATION

Operator

Welcome to the ScanSource quarterly earnings conference call. (Operator Instructions) Today's call is being recorded. If anyone has any objections, you may disconnect at this time.

I would now like to turn the call over to Mary Gentry, Senior Vice President, Finance and Treasurer. Please go ahead.

Mary Gentry - Scansource Inc - Senior Vice President, Treasurer and Investor Relations

Good morning, and thank you for joining us. Our call will include prepared remarks from Mike Baur, our Chair and CEO, and Steve Jones, our Chief Financial Officer. We'll review our operating results for the quarter, and then open the line for your questions. We posted an earnings infographic that accompanies our comments and webcast in the Investor Relations section of our website.

As you know, certain statements in our press release, infographic, and on this call are forward-looking and subject to risks and uncertainties that could cause actual results to differ materially from expectations. These risks and uncertainties include the factors identified in our earnings release, in our Form 10-K for the year ended June 30, 2025, and in our subsequent reports on Form 10-Q.

Forward-looking statements represent our views only as of today and ScanSource disclaims any duty to update these statements except as required by law. During our call, we'll discuss both GAAP and non-GAAP results. We've provided reconciliations on our webcast -- website and in the press release included in our Form 8-K filed earlier today.

I'll now turn the call over to Mike.

Michael Baur - Scansource Inc - Chairman of the Board, Chief Executive Officer

Thanks, Mary. And thanks to everyone for joining us today. Our team delivered strong third quarter results with adjusted EBITDA, EPS, free cash flow, and ROIC all increasing versus the prior year. I'm pleased to see improved hardware demand drove 9% growth in net sales, with growth across most technologies, but especially networking and security.

We believe end users have more choices than ever and solutions are getting more complex. But what they're really looking for are business outcomes, complete solutions, not point products. Research shows us that end users prefer to buy from trusted partners who can deliver across the full technology stack. That's why we're taking the next step to help our partners grow their business by launching a new converged communications business unit to deliver a unified One ScanSource partner experience.

This new business unit will include the business development and sales resources, pre-sales engineering, marketing, and supplier management functions, bringing together the ScanSource Specialty Communications team and the Intelisys CX cloud-based solutions team into one combined business unit. This team will support specialty communication VARs and Intelisys CX partners, helping VARs sell more cloud recurring revenue products and solutions and helping Intelisys partners attach more hardware.

Importantly, each partner will have dedicated sales resources to sell across our One ScanSource portfolio. The Converged Communications business unit will be led by Katherine White, who brings five years of ScanSource experience across both our specialty business and Intelisys.

Looking ahead, we're focused on helping our channel partners grow by delivering innovative converged solutions, including, of course, new opportunities in AI. Our partners are finding excellent opportunities for AI adoption in the CX solutions area.

Let me share two examples of recent AI channel wins. First, with AI as automation, a financial institution adopted an AI-powered platform with AI agents to handle routine inquiries. That freed up approximately four to five hours per live agent each week, so they could focus on more complex customer needs.

Second, with AI as augmentation, AI helps drive revenue expansion, including cross-selling. In this deployment, AI supports inside sales agents during live interactions by providing real-time recommendations.

We believe both examples highlight how ScanSource helps our partners bring converged AI-enabled CX solutions to market. Overall, our strong results this quarter reinforce our confidence in our business model as we look to the future.

I'll now turn the call over to Steve to take you through our financial results and our outlook for fiscal year 2026.

Steve Jones - Scansource Inc - Senior Executive Vice President, Chief Financial Officer

Thanks, Mike. We're pleased with our Q3 results, with consolidated net sales and non-GAAP EPS growing 9% year-over-year. We also delivered strong free cash flow in the quarter and feel very well positioned to deliver our fiscal year 2026 outlook.

Turning to our segments, I'll start with Specialty Technology Solutions. Net sales increased 9% year-over-year, led by North America hardware sales growth across most of our technologies. Gross profit increased 10% year-over-year to \$81 million.

Approximately 15% of segment gross profit is coming from recurring revenue, led by managed connectivity growth from our Advantix and DataXoom acquisitions. Segment adjusted EBITDA grew 6% year-over-year to \$24.7 million with an adjusted EBITDA margin of 3.3%.

In our Intelisys & Advisory segment, net sales declined 1% year-over-year. Intelisys annualized net billings increased to approximately \$2.88 billion. Quarter-over-quarter, both segment net sales and gross profits increased 4%. Adjusted EBITDA for the segment was \$11 million, a sequential quarter growth of 6%, with segment adjusted EBITDA margin of 42%.

Going a bit deeper on balance sheet and cash flow, we ended Q3 with \$120 million in cash and a net debt leverage ratio of approximately zero on a trailing twelve-month adjusted EBITDA basis. For the quarter, we generated \$69 million in free cash flow, bringing our year-to-date free cash flow to \$119 million.

Share repurchases totaled \$33 million in the quarter, and we had \$146 million remaining as of March 31, 2026, under our share repurchase authorization. Adjusted ROIC was 14.3% for the quarter and 13.6% year-to-date.

We continue to have a strong balance sheet, and we're well-positioned to execute our strategic priorities and achieve our three-year goals. Our three-year goals focus on growing the company's gross profit contributions from recurring revenue, expanding our profitability, delivering strong free cash flow, and maintaining disciplined capital deployment. You can find our goals in the infographic and our investor presentation in the Investor Relations section of our website.

We continue to explore acquisition opportunities that could expand our technology stack, our capabilities, and accelerate our recurring revenue growth. Our capital allocation priorities also include continued share repurchases. We are confident in our business model, and our Q3 results support our expectations for our annual outlook.

We are maintaining our full-year projections for both revenue and adjusted EBITDA, and for FY26 free cash flow, we are raising our expectations to at least \$90 million.

We'll now open it up for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Keith Housum, Northcoast Research.

Keith Housum - Northcoast Research - Research Analyst

Hey, Steve, in terms of the revenue guide for the full year, based on the strong core you have, if my math is right, that would suggest, at a top side, revenue growth of only 2% in the quarter and on the downside would be a decline of 10%. Was that intentional in terms of what you're thinking about for the second quarter or the next quarter?

Steve Jones - Scansource Inc - Senior Executive Vice President, Chief Financial Officer

Well, Keith, I'll tell you what. Thanks for the question, by the way. When we look at our full year outlook that we gave last quarter, we said that we would need some large deals coming in, and we had growth projected for the second half. Q3 delivered on that, and we're confident that we can deliver our full year guidance, but we don't want to get over our skis as we look at Q4.

Keith Housum - Northcoast Research - Research Analyst

Okay. Is there a sense that business was pulled forward from fourth quarter into third quarter based on, you know, the world that's in chaos when it comes to memory pricing right now?

Steve Jones - Scansource Inc - Senior Executive Vice President, Chief Financial Officer

What I would say on that, Keith, is the visibility is always hard on pull forwards and that kind of detail. But we don't believe that we saw material pull forwards in our Q3 results.

Keith Housum - Northcoast Research - Research Analyst

Okay. Appreciate it. You guys called out Resource sales being down in the quarter. I would assume those would sequentially grow every quarter. Was there anything unique that happened in the quarter that would cause that to be down?

Steve Jones - Scansource Inc - Senior Executive Vice President, Chief Financial Officer

Well, on Resourcive, remember, that's our end customer-facing business, and what you'll see in that is there's recurring revenue and there's services revenue in that business. Some of those services revenues can be up and down quarter-over-quarter.

Keith Housum - Northcoast Research - Research Analyst

Okay. Got you. How were Intelisys orders for the quarter? I know you guys mentioned billings were \$2.88. Well, how did the orders do?

Michael Baur - Scansource Inc - Chairman of the Board, Chief Executive Officer

Hey, Keith. It's Mike. Good morning. One of the things that we're focused on is how do we accelerate new order growth, and that's one reason we really are focusing on establishing this new group, this new team.

We believe that we need to put additional focus on new orders, especially through the VAR community. This converged communications team is going to have as a primary goal is how do we get more partners selling Intelisys and getting the new order growth to accelerate. We would like to see that grow faster.

Keith Housum - Northcoast Research - Research Analyst

I assume that order growth didn't grow for the quarter year over year?

Michael Baur - Scansource Inc - Chairman of the Board, Chief Executive Officer

No, we didn't say that. Our belief is that we are doing everything we've said we're going to do, but we want to go faster. We don't believe it's growing at the rate we would like to see.

Keith Housum - Northcoast Research - Research Analyst

Got you. It's the last question from me, and I'll turn it back over, but in terms of the STS segment, revenue was almost identical to the third quarter, but yet gross margins were 50 basis points higher. I know last quarter you guys called out freight costs due to more small and medium-sized businesses. Anything else that, you know, drove the improved gross profits for the quarter?

Steve Jones - Scansource Inc - Senior Executive Vice President, Chief Financial Officer

Keith, this is Steve. I would say it's more mix in that benefit. We've seen the freight cost normalize for us. We thought that that was going to be more of a one-time impact in the quarter. So I would say it's more of a mix story in terms of the improved margins.

Operator

Gregory Burns, Sidoti.

Gregory Burns - *Sidoti & Company LLC - Analyst*

Morning. Just to follow up on, you know, the investments you're making in the Intelisys side of the business to drive faster growth. I know, you announced this new, converged business unit, but you've done a number of things over the last 12 to 18 months to kind of stimulate that growth.

Are you finding, like, the impact of those, the impact of those investments and changes that you previously made are not what you expected them to be? Has there been, like, increased competitive response? Like, why haven't you been able to get the growth out of Intelisys where you think it should be?

Michael Baur - *Scansource Inc - Chairman of the Board, Chief Executive Officer*

Hey, Greg, it's Mike. Good morning. I think from my perspective, we've been very clear that we need to see acceleration of our new orders growth. We've been able to talk consistently over time about end user billings being also the indicator of how's our revenue going to come in.

New order growth, if you remember, has a lag between a new order and revenue for us. We clearly have to not only continue doing what we were doing for new orders, but everything that I'm talking about today that's new, we won't see the results of that for anywhere from 6 to 18 months. So really what I'm saying today is we're going to do more so that we can, a year from now, see even more of those results.

This is the I would say, the challenge with our Intelisys business is what we're seeing in new order growth now were actions we took a year ago. And we're saying we'd like to see better results. We want to accelerate that. And we believe now is the time.

One more point, Greg, is we felt like we needed to get to this point in the year, the fiscal year, to make some of those decisions. When we said back in August that our strategy and our outlook for the year was X, we said we got to have a strong second half. Some of our decisions would not be made for no more investments until we got through the first half. Well, we're there, and we saw what happened in Q3, and so we have the confidence that we should do that now. That's why now it's a timing question for us.

Operator

(Operator Instructions) Logan Katzman, Raymond James.

Logan Katzman - *Raymond James - Analyst*

This is Logan Katzman on for Adam Tindle. Maybe back to one of the first questions that was asked earlier. When we're looking into 2027, since we have to start to model that, I guess first any guidelines or parameters you guys want to maybe give us as we look into modeling that?

And secondly, maybe what do customer conversations look like in that around the first half of 2027? I know it's a little early, but kind of back to the polling question. Just curious if you're seeing a big drop-off here potentially in demand as we move into that first half '27 to each calendar '26. Just wanted to see what you guys were hearing on that front. Thank you.

Steve Jones - *Scansource Inc - Senior Executive Vice President, Chief Financial Officer*

Yeah, Logan, thanks for the question. I would just first start out by saying we haven't given '27 guidance yet. We typically would do that when we deliver our fourth quarter results. So we're a little bit early in talking about FY27 for us. We're happy with where Q3 came in. We're confident in our Q4 forecast that builds to our full year guidance that we've given the guidance range.

There's some things in our business right now that have a lot of momentum. Mike talked about security and networking having a lot of momentum from a sales perspective. What we saw this quarter that we haven't seen in previous quarters is most of our technologies show growth, which that's a great sign for us, as we think about going into 2027, is to have that momentum.

Logan Katzman - *Raymond James - Analyst*

Awesome. I appreciate the color. Thank you.

Operator

Thank you. I would now like to turn the conference back to Steve Jones for closing remarks. Sir?

Steve Jones - *Scansource Inc - Senior Executive Vice President, Chief Financial Officer*

Yeah. Thank you for joining us today. We expect to hold our next conference call to discuss our June 30th quarterly and full fiscal year results on Thursday, August 20th at approximately 10:30 AM.

Operator

This concludes today's conference call. Thank you for participating. You may now disconnect.

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