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PRESENTATION

Operator

Good day, ladies and gentlemen, and welcome to the Gentex Fourth Quarter 2017 and Year-End Earnings Conference Call. (Operator Instructions) I would now like to turn the conference over to your host, Josh O'Berski, Gentex's Investor Relations Manager. Sir, you may begin.

Josh O'Berski

Thank you. Good morning, and welcome to the Gentex Corporation Fourth Quarter 2017 Earnings Release Conference Call. I'm Josh O'Berski, Gentex' Investor Relations Manager, and I'm joined by Steve Downing, President and CEO; Kevin Nash, Vice President and Chief Accounting Officer; and Neil Boehm, Vice President of Engineering. This call is live on the Internet by way of an icon on the Gentex website at www.gentex.com.

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This conference call contains forward-looking information within the meaning of the Gentex Safe Harbor statement included in the Gentex Reports Fourth Quarter and Year-End 2017 Financial Results press release from earlier this morning and as always, shown on the Gentex website. Your participation in this conference call implies consent to these terms.

Now I'll turn the call over to Steve Downing, who will give the fourth quarter 2017 financial summary. Steve?

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Thank you, Josh. For the fourth quarter of 2017, the company reported net sales of $459.6 million, an increase of 9% compared to net sales of $419.9 million for the fourth quarter of 2016. The increase was primarily due to a 13% increase in auto-dimming interior and exterior rearview mirror shipments on a quarter-over-quarter basis. For calendar year 2017, the company's net sales increased 7% to $1.79 billion compared to $1.68 billion for calendar year 2016, primarily as a result of a 9% increase in auto-dimming interior and exterior mirror unit shipments.

The gross profit margin in the fourth quarter of 2017 was 39.2% compared with a gross profit margin of 40.3% in the fourth quarter of 2016. The gross profit margin headwind on a quarter-over-quarter basis was primarily due to annual customer price reductions that were not fully offset with purchasing cost reductions. The quarter-over-quarter comparisons were also negatively impacted because of unusually strong advanced feature mix in the fourth quarter of 2016 related to certain previously disclosed supply constraints experienced at the end of 2016 that negatively impacted base mirror shipments.

For calendar year 2017, the gross profit margin was 38.7% compared with a gross profit margin of 39.8% for calendar year '16, driven downward by annual customer price reductions, higher fixed overhead costs and negative product mix, which were not fully offset by purchasing cost reductions. However, we are very pleased to see a solid rebound in revenue and unit growth during the fourth quarter of 2017 and to see continued gross margin improvement during the second half of the year despite the fact that we have been battling against difficult comparisons in product mix and our typical annual price reductions.

Operating expenses during the fourth quarter of 2017 were up 12% to $46.3 million when compared to operating expenses of $41.2 million in the fourth quarter of 2016. Operating expenses in the fourth quarter of 2017 included approximately $4.4 million of certain costs associated with the previously announced retirement of the company's former CEO. For calendar year 2017, operating expenses were $171.2 million, up 9% compared to $156.7 million in calendar year 2016.

During the fourth quarter of 2017, the company's effective tax rate was 5.6%, down from 31.2% during the fourth quarter of 2016, primarily driven by the impacts of the Tax Cuts and Jobs Act of 2017. The lower effective tax rate was due to the remeasurement of the company's deferred tax liabilities, which was partially offset by the company's net transition tax. The total impact of the tax adjustments reduced the company's income tax expense during the quarter by $37.2 million. The company's effective tax rate for calendar year 2017 was 23.5%, which was down from 31.9% for calendar year 2016 due to the impacts of the Tax Cuts and Jobs Act of 2017.

Net income for the fourth quarter of 2017 was up 47% to $130.5 million when compared to net income of $88.8 million in the fourth quarter of 2016, primarily driven by the lower effective tax rate as well as the 9% increase in revenue on a quarter-over-quarter basis. Net income for calendar year 2017 was $406.8 million, up 17% compared with net income of $347.6 million in calendar year 2016, also driven by the lower effective tax rate and a 7% increase in revenue on a year-over-year basis.

Earnings per diluted share in the fourth quarter of 2017 were $0.46, representing an increase of 48% when compared with earnings per diluted share of $0.31 in the fourth quarter of 2016. Earnings were positively impacted by $0.13 per diluted share during the quarter as a result of the previously mentioned tax benefits. For calendar year 2017, earnings per diluted share were $1.41, an 18% increase year-over-year compared with $1.19 for calendar year 2016. The 2017 calendar year earnings include $0.13 per diluted share as a result of the previously mentioned tax benefits.

The company repurchased 5.1 million shares of its common stock during the fourth quarter of 2017 at an average price of $19.96 per share. For the year ended December 31, 2017, the company repurchased 12 million shares of its common stock at an average price of $19.35 per share. Total share repurchases increased 17% when compared to the 10.3 million shares repurchased for the year ended December 31, 2016, both of which were in accordance with the company's existing share repurchase plan. As of December 31, 2017, the company has 9.8 million shares remaining available for repurchase in the previously announced plan.

Additionally, on January 16, 2018, the company repurchased and subsequently retired approximately 5.5 million shares of common stock from the former CEO pursuant to his previously disclosed retirement agreement, which was effective December 31, 2017, at an average price of $20.98 per share. These share repurchases were approved by the company's Board of Directors and were not repurchased as part of the company's existing share repurchase plan. Therefore, the repurchase of these shares does not affect the calculation of remaining shares available for repurchase for the company's existing share repurchase plan.

The company remains optimistic about its future forecast and cash flow prospects and as a result, currently plans to continue to repurchase additional shares of its common stock in the future depending on macroeconomic issues, overall market trends and the anti-dilutive impact of share repurchases, along with other factors that the company deems appropriate.

The company paid down $28.9 million on its term loan during the fourth quarter of 2017 for a total of $107.6 million during the calendar year 2017. The company expects to continue at its discretion based on previously disclosed factors to pay additional principal towards its debt in the future in anticipation of such debt maturing on September 27, 2018.

I'll now hand the call to Kevin Nash with fourth quarter 2017 financial details.

Kevin C. Nash - *Gentex Corporation - CAO and VP of Accounting*

Thank you, Steve. The following balance sheet items represent a comparison versus December 31, 2016. Cash and cash equivalents were $569.8 million, up $23.2 million from $546.5 million, primarily due to cash flow from operations but were partially offset by share repurchases, accelerated debt repayments, capital expenditures and dividends. Short-term investments were $152.5 million, down from $177 million, and long-term investments were $57.8 million compared to $49.9 million.

Accounts receivable was $231.1 million, up from $211.6 million, primarily due to the higher sales levels on a year-over-year basis. Prepaid expenses and other were $14.4 million, down $16.2 million, primarily due to reduced refundable income taxes versus December 31, 2016.

Inventories were $216.8 million, up from $189.3 million, primarily due to extended lead times on certain electronics and raw material inventory levels to support first quarter of 2018 production and sales forecast. Accounts payable increased to $89.9 million from $80 million. Accrued liabilities were $153.8 million, up from $69.9 million, primarily due to the reclassification of the company's long-term debt to short-term debt as a result of the September 2018 maturity.

Now for a couple of cash flow highlights. Fourth quarter 2017 cash flow from operations was $145.1 million versus $120.6 million in the fourth quarter of 2016, driven by changes in net income and deferred taxes and fluctuations in working capital. And calendar year 2017 cash flow from operations was $497.7 million versus $477 million in calendar year 2016, which was also driven by increases in net income as well as changes in deferred taxes and working capital.

CapEx for the fourth quarter was $17.9 million compared with $29.5 million for the fourth quarter of 2016. And calendar year 2017 capital expenditures were $104 million compared with $120.9 million for calendar year 2016. And depreciation and amortization for the fourth quarter was $24.7 million compared with $19.7 million in the fourth quarter of 2016. And calendar year 2017 depreciation and amortization was $99.6 million compared with $88.6 million for calendar year 2016.

I'll now hand the call back over to Steve for a business development update.

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Thanks, Kevin. The last couple of months have been a very active period for the company. Beginning at SEMA in November, Gentex debuted a new aftermarket version of our Full Display Mirror that is capable of handling multiple camera feeds to allow for split-screen applications designed to help rearward visibility. Additionally, we showcased the design concept for our SmartBeam lighting control technology. This new concept showed a reduced package-sized control module that can be incorporated as either a standalone module for the automotive aftermarket or be packaged within a headlamp module for use in motorcycles, ATVs or jeeps.

Our effort continued in the CES in January where the company, through a series of press releases, announced new relationships with technology partners, debuted several new technologies and demonstrated through our custom developed product demonstrator, new use cases for existing Gentex products as well as forward-thinking concepts that leverage fundamental Gentex technology. All of this work was done to help showcase for our customers and investors the role we believe Gentex products can play in cars today as well as in the car of the future.

An important building block of our new product offering for this year's CES was built on the expanding relationships Gentex is developing with other technology companies. Our first example of this came from one of the key new products Gentex debuted at CES, which was an extension of our current HomeLink product to include home automation functionality. This new product's official name is HomeLink Connect.

Gentex announced prior to CES that we have participated in a round of financing with Yonomi, our partner in home automation technology. This round of financing not only established an equity position for Gentex and Yonomi but will also help fund Yonomi as they work to stay a market leader in the home automation space.

Gentex utilized Yonomi as our home automation aggregation partner and combined it with a Gentex-developed app and cloud infrastructure to show a HomeLink app running on the center stack of a Land Rover Velar. The most exciting piece of information about this new product came later in a joint press release with Jaguar Land Rover where we announced that they are planning to be the first OEM to deploy this new technology on their vehicles.

A second example of Gentex partnership on new technology was announced during the show when Gentex completed a licensing agreement with Fingerprint to deploy iris scanning biometric technology in automotive applications. This year at CES, Gentex showed a functional and seamless integration of this iris scanning technology in our all-new product demonstrator. The product demonstrator leveraged the iris-based biometric solution to show in-vehicle authentication and show use cases to an OEM that includes security, vehicle personalization and customization, home automation control and vehicle-to-infrastructure transactions.

Our third example of a new Gentex partnership was included in a CES press release that highlighted the work the company has been doing with Visa to provide concepts on how to make it a transactional car a reality. The Gentex product demonstrator showed how biometrics will be a critical part of the ecosystem in the car of the future and how a connected car that has authenticated a driver can leverage transactional technology through our development partnership with Visa.

These 3 examples are indicative of the work the company has been doing to help expand our product offering by leveraging our existing technology, location in the vehicle and core competencies that have made Gentex successful in the past and will continue to do so in the future.

I'm now going to turn the call over to Neil Boehm, and he's going to spend a few minutes describing the product showcased at CES.

Neil Boehm - *Gentex Corporation - VP of Engineering*

Thank you, Steve. As Steve mentioned, CES 2018 was a great platform for Gentex to showcase the evolution of concepts we showed at CES 2017 as well as introduce new innovative technologies that can help drive future growth.

One of the proof of concepts we demonstrated was a camera monitoring system on a 2018 Volvo XC90 to show how cameras and mirrors can coexist, enabling the consumer to choose which technology is most conducive, safe and comfortable to use during driving. The system we displayed had 3 cameras, 1 in the shark fin antenna on the roof of the vehicle and the other 2 were in the outside mirrors behind the auto-dimming glass.

The video from these 3 cameras was then processed and displayed on a Full Display Mirror with various user-selectable views that allows the driver to choose the display format they're most comfortable with when in display mode. This proof of concept demonstrated 4 unique aspects that we believe separate our system from any competitive products.

First, during normal viewing of the outside mirror, the camera is not visible. Gentex is leveraging our experience with thin film coatings that allow the camera to see through the reflective surface of an auto-dimming mirror and still utilize the mirror surface to meet field-of-view requirements.

Second, our system proved out the concept and the ability to have a camera behind an auto-dimming device without compromising the camera performance or coloration of the displayed image while the outside mirror is darkening.

Third, this new mirror system included a newly redesigned, fully compliant outside auto-dimming mirror in a smaller form factor to improve fuel economy while adding more capability.

And lastly, the hybrid mirror solution on the XC90 that was on display meets the field-of-view requirements in both Europe and North America, allowing an OEM to design a vehicle to include mirrors and/or digital displays for camera monitoring systems in one design and hardware set.

Additionally, at our booth, we showed a demonstration property called the immersive product display, IPD. This property allowed customers to sit inside and view how we see the car of the future and how Gentex technologies will be relevant. The immersive product display tour began with a walk around the outside of the demonstrator so that viewers could take note of how dimmable glass technology is applicable to various locations in the vehicle of the future.

There were 7 unique dimming devices: a dimmable combination HUD to help improve the display contrast of pop-up HUD images; 2 unique dimmable cover devices, one to cover and conceal sensors and one to hide the map lamps when not in use; a dimmable visor positioned above the mirror to help create contrast and control light flow into the vehicle; 2 dimmable roof panels above the driver and passenger position; a dimmable back window; and our Full Display Mirror and exterior mirrors, all featuring dimmable technology. We believe that our experience in automotive auto-dimming technology positions us well for these potential new applications.

Once inside the IPD, we were able to showcase a functional version of the iris scanning biometric system to registered users. Once registered, the IPD led the user through a scenario of demonstrations that showcased Gentex's vehicle customization and security scenarios, HomeLink and HomeLink Connect home automation technology, Integrated Toll Module systems and in-vehicle payment systems through a relationship with Visa. We believe our new IPD concept was the most comprehensive and overthinking product strategy demonstration ever produced by the company.

Now for an update on our Full Display Mirror launches and activity. We are pleased to announce that during the fourth quarter of 2017, we began shipping our Full Display Mirror to Toyota, our fourth OEM, on both the Lexus LS and Toyota Alphard in the Japan market. Toyota has been a great partner in the development of technologies over the last several years, and we're excited to see them launch on these vehicles.

Also in the fourth quarter of 2017, we began shipping the Full Display Mirror for the INFINITI QX80. This is our second vehicle platform at Nissan. With the 4 announced OEMs, Gentex is currently shipping Full Display Mirror products on 14 different platforms in various global markets.

At CES 2018, Gentex also announced that our fifth OEM for Full Display Mirror was Jaguar Land Rover. This is significant for us, being it's our first European OEM to implement the Full Display Mirror technology.

Finally, we are excited to announce that we have recently been sourced a Full Display Mirror program with our sixth OEM. This award helps to show the value our customers see in the combination of our auto-dimming and digital display technology.

I will now hand the call back over to Steve for the 2018 and 2019 guidance and closing remarks.

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Thanks, Neil. Our forecasted guidance for calendar years 2018 and 2019 are based on the mid-January 2018 IHS production forecast for light vehicles produced in North America, Europe and Japan and Korea. The current IHS production forecast for these markets is expected to be flat to down for both years. And based on that, the company estimates that net sales for calendar year 2018 will be between $1.89 billion and $1.97 billion.

The company estimates that the gross profit margin for calendar year 2018 will be between 38% and 39%. From an operating expense standpoint, the company expects ER&D and SG&A expenses to be between $180 million and $190 million for calendar year 2018.

Based on the recently passed Tax Cuts and Jobs Act of 2017, the company currently is estimating its annual effective tax rate to be between 18% and 21% for calendar year 2018. In order to support future growth and program launches, capacity expansion and production automation, the company estimates that capital expenditures for 2018 will be between $115 million and $130 million, and depreciation and amortization expense is estimated to be between $105 million and $115 million for calendar year 2018.

Based on the company's forecast for light vehicle production for calendar year '19, the company currently expects 2019 revenue growth of approximately 5% to 10% above the 2018 revenue estimates. The next 2 years present many challenges due to the flat-to-down light vehicle production environment, but we are currently forecasting solid revenue growth for both 2018 and 2019.

Thank you for your time, and we can now proceed to questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Chris Van Horn with B. Riley FBR.

Christopher Ralph Van Horn - *B. Riley FBR, Inc., Research Division - Analyst*

Steve, let me just say congratulations on the new role and fantastic quarter.

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Thanks, Chris. I appreciate that.

Christopher Ralph Van Horn - *B. Riley FBR, Inc., Research Division - Analyst*

So just on the guidance, continued execution above underlying production and the kind of 500 to 1,000 basis point growth. Just what are the puts and takes on that 5% to 10%? Is it what you see in the backlog? Is it take rates? What are kind of the mitigating factors there?

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Sure. Well, first, I think, on the -- the first thing we look at is not only the production levels but the mix in each of the regions. And so when you look through kind of of that, North American and European markets especially, and you look at historically, we've been a little more biased towards C, D and E segment and obviously, a lot less in the A and B. And so you have to look at not only where is growth happening in each region but where is that growth coming from. If you look at a lot of our international shipments, we had a lot of growth in base mirrors this quarter and really for the year. And so a lot of that is Gentex starting to expand under those new market segments, so A and B segment. And a lot of growth that's available to the company is coming from those smaller cars that historically have not been a part of our product mix. On the ASP side, what you're looking at is obviously the further penetration that Neil described in Full Display Mirror applications. And with what we showed at CES this year, we believe there's a very positive story around that execution. Obviously, the announcement today of our sixth OEM that we received, the sourcing for that application. So really pretty excited about the long-term growth aspects of the company. So there's a lot of variables that go into that. Obviously, the one that we like to look at is not only is there our content growth story, but there's our core products. In other words, inside and outside, auto-dimming base mirrors continue to show a very strong growth profile. And we think that's an interesting play for us longer-term as we continue to grow that real estate and geography. It gives us the opportunity to add more electronic content longer term.

Christopher Ralph Van Horn - *B. Riley FBR, Inc., Research Division - Analyst*

Okay, great. And then obviously, a number of new products that we saw at CES obviously look exciting. Could you give us a little bit of the timing perspective on some of them and then maybe some feedback you heard from the OEMs on the technologies that they saw?

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Yes. I think first, on the feedback side, what was interesting and -- for Chris, you were there, you saw a lot of it firsthand. When you roll out new products, Gentex has done a better job the last 2 years especially and this year was probably the furthest that we've ever taken it in terms of showing forward-thinking product strategy that's out 3 to 5 years. In other words, these concepts, we're capable of building, some of them today, some of them were products that we're in development on and are going to take a few years to finish up development. And so showing our customers what we believe can be relevant for them in a 3- to 5-year out time period is really a big leap for the company and something that we felt like we needed to do to position the company for that long-term growth prospects. And so those are really the kind of the horizon. If you look at the customer feedback, I think it was interesting. We had a tremendous amount of traffic, a lot of OEMs were very curious about how we were showing our products and how those products can be relevant on a car you're building and selling today or in a vehicle that you're going to sell in 10 or 15 years. And whether that's a driver-based vehicle or a rider-based vehicle on a fully autonomous environment, a lot of our technology we believe will be relevant in both of those vehicle markets.

Christopher Ralph Van Horn - *B. Riley FBR, Inc., Research Division - Analyst*

Okay, great. And then just one last one for me. And I apologize if I missed it. Did you highlight the net new launches for the quarter for the fourth quarter? And then possibly the percent of revenue from advanced features for the quarter?

Kevin C. Nash - *Gentex Corporation - CAO and VP of Accounting*

We didn't, Chris, on the net. There was a net 11 for the quarter, which is right in line with our average of all our 4 quarters. And then on -- we saw a similar mix is what we saw most of the year, Chris, on the base versus advanced feature. It was in the 54% to 55% of unit shipments. But as Full Display Mirror takes up, it helps on the revenue side to help balance that.

Operator

Our next question comes from Rich Kwas with Wells Fargo Securities.

Richard Michael Kwas - *Wells Fargo Securities, LLC, Research Division - MD & Senior Equity Research Analyst*

Steve, on the gross margin outlook. So the guide at the midpoint is a little bit below the number for the margin for 2017. You had some commodity headwinds versus productivity through most of '17. What's kind of baked into the outlook? Is that still a headwind in '18? Is there mix assumptions in there? How should we think about that? What kind of would move you to the high end of the 39% versus being at the low-end 38%.

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Well, I think first, yes, you're right, you're going to see -- well, we should go back and say '16, we had talked about it at that time, the mix was disproportionately strong. Primarily because of a supply shortage, we couldn't ship all of our base inside auto-dimming mirrors that we had wanted to ship at the end of '16. Obviously, that drove mix to improve. But that was an artificial improvement at the end of '16. It was higher than expected and higher than sustainable. If you look into '18, we're going to see some continued pressure on the commodity side. And really, what we're seeing, especially on the core electronics. So we're talking capacitors, transistors, resistors. There's a lot of supply constraints out there. And usually, what happens with supply constraints is you start to see some pricing pressure, at least not as much price reductions as we'd have normally forecasted or expected. So those are going to be a bit of a headwind. Obviously, with some of the growth and some of the new awards and advanced technology, that comes with slightly higher APR levels from us to the customer. And so when we add those altogether, that's kind we end up with that forecast. If you look at what can drive you to the low end or the high end, for us, it's primarily driven by around growth rates. If we were at the high end of that growth rate range, we'd expect to be at the high end of the margin range. Obviously, mix plays a big factor in that throughout the year. It's hard to predict base mirrors versus advanced feature and what customers are going to take, but those are the primary contributors.

Richard Michael Kwas - *Wells Fargo Securities, LLC, Research Division - MD & Senior Equity Research Analyst*

Is the assumption that the base, this base 54%, 55% is embedded in the assumption for gross margin for '18?

Kevin C. Nash - *Gentex Corporation - CAO and VP of Accounting*

I think what we're seeing so far is that revenue is going to be the driver and unit mix is not going to grow as much, so it sits pretty well. But like Steve said, when you start to get a little bit squeezed on the supply side, that's where the margin squeeze ends up happening. So I think we feel pretty good about where the mix is happening. It's still going to be in that same percentage range. But the ASPs, as you know well, on FDM growth, help overweigh some of the base mirror unit growth.

Richard Michael Kwas - *Wells Fargo Securities, LLC, Research Division - MD & Senior Equity Research Analyst*

Okay. And then just on tax, with regards to being below the 21% corporate, are you getting some benefit from the foreign-derived intangible income provision?

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Yes. So there's 2 things: the R&D tax credit, which we've always taken advantage of, that's still in play; and then the FDII, as you mentioned, it's still unknown. That's why we have a fairly wide range and there's a lot of work to do. But yes, that's the other piece of the benefit that gets us below 21% if, in fact, we do.

Richard Michael Kwas - *Wells Fargo Securities, LLC, Research Division - MD & Senior Equity Research Analyst*

Is there any offsets within this 18% to 21% that were profits versus last year that mitigated some of the downside?

Kevin C. Nash - *Gentex Corporation - CAO and VP of Accounting*

No. Well, the onetime cost for the transition tax was baked into the 37.2% that we talked about. But on an ongoing basis, yes, the manufacturing deduction is one thing that we did have before they got us from the 35% down to our 32% range. That's no longer in play. But obviously, you see the net benefit is still good.

Richard Michael Kwas - *Wells Fargo Securities, LLC, Research Division - MD & Senior Equity Research Analyst*

Great, okay. And then Steve, just big picture. So with the cash balance still well above $500 million, you got debt that's going to come off the books later this year, the cash flow profile is good. Yes, just what are your early thoughts around leveraging the balance sheet a little more, utilizing it more? And I know M&A has been a more focal point. You haven't done much here. But I mean, now it's been more a focal point on your end. But how should we think about this over the next 2, 3, 4 years around capital deployment and what your early thoughts are?

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Sure. Well, if you look at it, I think you summarized it very well. When you look at the discipline the management team has put in place driving revenue but then being disciplined about that income statement to make sure we're driving that all the way through the bottom line, that opens up a lot of opportunities for us as a company. What our goal is, is to take the vast majority of that free cash flow off the income statement and redeploy that into either acquisitions or share repurchases, things that we believe will provide significant long-term value for our shareholders.

Operator

Our next question comes from Ryan Brinkman with J.P. Morgan.

Ryan J. Brinkman - *JP Morgan Chase & Co, Research Division - Senior Equity Research Analyst*

I think this question was just explored some. But maybe looking for you to expand upon it a little, which is -- firstly, I must say congrats on the promotion, Steve. I think it's very well deserved. But really, what I'm trying to figure out and I think with the last question, was driving home to as well was -- because Gentex has only ever really had 1 CEO before, how much of like how the company has been run in general and how it's been capitalized as a function of what you might call like Gentex DNA versus maybe Fred Bauer's sort of personal leadership style and management philosophy, that style, it's included a strong focus on organic growth, less focus on inorganic growth. I recognize there has been some focus on share repurchases, but like you just said kind of funded through free cash flow, less focused on leverage, specifically to repurchase shares. Although I recognized you have taken on some leverage in conjunction with HomeLink. So maybe said differently is like what should investors think about as staying the same under your leadership versus may be potentially changing?

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Sure. I think if you look at the core DNA of the company, it's much in line with the way we've operated in the past. In other words, I always joke about it being more of a Midwestern values philosophy, right? In other words, having a little bit of a skeptical eye towards leverage, more focused primarily on organic growth, driving value, using the free cash flow that we generate off of that business to help us in -- whether it's share repurchases or acquisitions. It doesn't mean we're completely opposed to the concept of leverage as we showed in the HomeLink acquisition a few years ago. But our preference is to use what we already have to keep the company kind of in line with that philosophy. Now what you will see change, and we have been changing really for the last few years, is that consistent share repurchase philosophy, and that's been ramping up over the last 2 years especially. If you look at Q4, we'll look at that annualized run rate, you look at what we did already with the purchases we announced in Q1, that's absolutely going to be a part of the company's philosophy going forward, is making sure that we are using that cash we generate off the business that if we can't find a business that fits really well with us, that we can acquire, that helps drive shareholder value, that we feel comfortable with the business prospects of the acquisition, that we're happy to continue to buy Gentex stock back. We look at our long-term growth prospects, and we say it's a fair price right now. And we believe we're going to continue to show that we're interested in buying back our own stock at these price levels.

Ryan J. Brinkman - *JP Morgan Chase & Co, Research Division - Senior Equity Research Analyst*

That's very helpful. And I guess, just the last question is when you think about expansion into like the aerospace industry, I mean, you've already done this via your core auto-dimming technology. But in the car, you started to do things that are really unrelated to auto-dimming and unrelated to electrochromatism and even mirrors with HomeLink, et cetera. I'm just curious if we should think about you maybe expanding beyond auto-dimming when you go to other industries too.

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Yes, I think longer-term, our primary focus in a new industry is to take known existing technologies and leverage them into that new industry. Beyond that, we're going to take the rest of our core competencies and we -- if you look at our beginning of our slide deck on the IR side, you'll see we kind of changed that philosophy less -- from a few years ago, less from just saying we're not a dimming company to saying we're a thin films company, a chemistry company, an electronics and microelectronics and software company. More importantly, when you can combine a few of those attributes together into a single product, we believe it gives us a very unique platform to compete from. So as you -- as we move forward, a lot of what you saw at CES this year was focused on taking those core competencies and deploying them in different ways. And sometimes that means forming a partnership or a license agreement with another technology that joins really well with our existing geography and platform. And we are pretty excited about the growth prospects those type of applications bring forward for us.

Operator

Our next question comes from David Whiston with MorningStar.

David Whiston - *Morningstar Inc., Research Division - Strategist*

I want to start with HomeLink Connect. One thing I wasn't totally clear on when I read about it was, can it integrate with another digital assistant IoT platform, just Alexa or NAS? Or is a service for me entirely, within the Gentex Yonomi product suite?

Neil Boehm - *Gentex Corporation - VP of Engineering*

No, the plan is for that to be expanded and capable to interface with all of those IoT devices as we continue to roll out the platforms.

David Whiston - *Morningstar Inc., Research Division - Strategist*

Okay. And on biometrics, are you having discussions with your customers or potential customers where this technology could be anywhere in the vehicle interior or even exterior? Or is it more based on where today the mirror and center stack are?

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Well, yes, we're open to the concept of this technology residing in multiple geographies in the vehicle environment. It just so happened, one of the advantages Gentex brings is that our geography is actually pretty conducive to what we're trying to do. That mere upper windshield area is a very good place for that type of technology. So a lot of -- and initially, we can build prototypes and proof of concepts much quicker in our own geography. So that's kind of our go-to-market philosophy, but we're not dependent on that one geography or that one location in order to be willing to sell this type of product into the automotive space.

Neil Boehm - *Gentex Corporation - VP of Engineering*

Yes. And we didn't touch it in the discussions, but we had a press release as well around CES where we've put an iris detection system in a vehicle, a Rinspeed vehicle called the Snap concept car, where it was positioned -- it's an autonomous car, no steering, there's no mirror, so it's positioned in various locations to authenticate who people are when they get in the vehicle.

David Whiston - *Morningstar Inc., Research Division - Strategist*

And on FDM, did I hear -- were those wins with Toyota, Lexus, they were only in Japan?

Neil Boehm - *Gentex Corporation - VP of Engineering*

They are currently in the Japan market, correct.

David Whiston - *Morningstar Inc., Research Division - Strategist*

Okay. Are you optimistic you could get some Toyota platform business in the United States?

Neil Boehm - *Gentex Corporation - VP of Engineering*

We are optimistic that, that's a great potential.

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

We're open...

Operator

Our next question comes from Anthony Deem with Longbow Research.

Anthony J. Deem - *Longbow Research LLC - Senior Analyst*

So looking at your 2018 guide, it implies 8% to 14% operating cost growth when I'm stripping out the $4.5 million retirement cost. So I'm just wondering if you could provide some detail exactly what's driving that cost materially higher? Because historically, Gentex manages operating cost inflation in line or below revenue growth. So I'm just wondering, is there conservatism? Are there ongoing costs related to Mr. Bauer or something else we should think about?

Kevin C. Nash - *Gentex Corporation - CAO and VP of Accounting*

No, I think -- thanks for the comment. But it's really driven around growth in our R&D platform. Some of that stuff that you saw at CES, Anthony, is driven by increasing our development budget, but then also being more present in our business development strategy. We're trying to grow out the aerospace business. We continue to work in areas beyond just the automotive space. And so we're starting to add resources to help support future growth. And then the cost of some of these trade shows and those things, while not individually material, start to combine in there. So it's really a combination of all those things put together because we're focused on that future like Steve talked about and the things we talked about in the press release earlier.

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

And remember, the equity has always been a big part of management compensation for all of our management team here. And so as the stock does continue to increase, that does have a more expensive -- a more expense impact on the R&D and SG&A portions of the income statement.

Anthony J. Deem - *Longbow Research LLC - Senior Analyst*

Okay. Then the #1 question I've been getting on Gentex is the margin profile of your business longer term and 2018 obviously looks great. But can you help us better appreciate why OEMs may or may not target more aggressive price downs in your portfolio of products versus what we've seen historically? Because I mean, look, my understanding is OEMs also make a very healthy margin off your products. So do you think they'll disproportionately target higher-margin suppliers like yours perhaps to subsidize some of their R&D development efforts or other things?

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Yes, I think that's probably -- that's a great question because it gives us a chance to talk about one of the bare cases that is out there on Gentex, and that is that we can't maintain this profit margin or profile. If you back up a few years, we were down to 32.5% gross margin range. We've worked really hard as a team to get that back up to this level. And how we accomplished that is investing in new products and technologies. If the product doesn't change, the margin will erode. That is just the facts of the industry and the facts of any type of product that's getting long in the tooth. What you've seen is Gentex invest in a whole different product offering. And those new product offerings, they come with R&D expenses like you asked about earlier. But then they also open up the opportunity for better pricing profiles for our customers with their consumers. And whenever that happens, we can build a business case together. It does lengthen the cycle and it opens up the opportunity for higher margins. Additionally, when you start talking about new markets and new industries, you're leveraging existing overhead to hopefully create revenue that's using that same operational expense. And so we're continuing to look for ways to expand our markets to get operationally improved. And we'll look at automation and the things we do in the back of the house to try to make sure that we keep our costs in line. And so when you look at our history, really, over the last 15 years, then you start to see a very different story, not of the story of where it's peaked and it can only go down, but where we've had rough patches where the product offering didn't offer out the margin profile and we've worked really hard to correct that.

Anthony J. Deem - *Longbow Research LLC - Senior Analyst*

Very good. If I could just ask one more here. I think implied in your gross margin comments, maybe the advanced feature mix might have been a little weaker year-over-year. I think looking back, 60% was a number in the fourth quarter '16. So did you provide that advanced feature number specifically for fourth quarter '17 here? And then just secondly, if I think about 2018, first quarter '17, we're at 50% advanced feature mix. But second quarter, third quarter, you jumped to 60% plus. So just for modeling purposes and the cadence of gross margins, should I model first quarter, fourth quarter gross margins potentially stronger versus second quarter, third quarter because of maybe difficult mix comps? Or do you see yourselves matching that strong mix in subsequent quarters from an advanced feature perspective?

Kevin C. Nash - *Gentex Corporation - CAO and VP of Accounting*

Yes, so really what we've been talking about, most of the year was about a 55-45 split from a base versus advanced feature mix. And I think going into '18, we see it fairly similar. The one thing that does impact that as we continue to grow the FDM side, that feature has better pricing and really good profitability versus most of our historical features. And some of the other things that are historically base level, we are converting a lot of our base level product from our old bezeled products to chrome ring in our higher ASP product there. So that's actually helping the revenue side while not the unit growth. And so Anthony, I don't think that things are going to outgrow -- that makes me say it's fairly similar. But with the growth profile of the different products altogether, I think we feel pretty good about that margin profile throughout calendar '18.

Operator

Our next question comes from David Leiker with Baird.

Joseph D. Vruwink - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Associate*

This is Joe Vruwink for David. Can you maybe compare and contrast FDM relative to some of your other electronic feature launches? I'm thinking about RCD and SmartBeam back in the day, both really successful products. I think both had about 1 million units of volume within 5 or 6 years from launch. It seems like FDM though actually has better global participation. It's launching everywhere, pretty diverse customer set. So is FDM on its way to being a 1 million unit product? I know you've guided to 2020. But in the early 2020s, that type of volume is possible?

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

We hope so. I think the market interest tells us that, that's absolutely possible. Part of that is going to be a factor of doing what Gentex has historically done really well, and that is keep evolving that technology. And one of the things we didn't really talk about today in the conference call is we showed a Gen 2.5 version at CES as well. And I think when you see that product and you compare to the Gen 1 product, you start to see the leaps and improvement in technology. And then of course, from a marketing standpoint, how that will help the OEM with their consumers. So we look if we continue to invest in that product and do the things we need to do to keep that product fresh and new, we believe those are absolutely realistic growth targets. If you try to compare them to those other products, I'd say you're absolutely right. SmartBeam for us was a big step forward because it really brought in the European market, which hadn't been the case for us historically. Most of our products and technology had been focused on the North American market because quite frankly, it's where we lived and most of our engineering resources were. SmartBeam changed that and we think FDM changes that even more. If you look at visibility or rearview, that's a global issue. And we believe technology is best-in-class as it relates to answering those technical issues.

Joseph D. Vruwink - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Associate*

And because you brought up Gen 2.5, so RCD ultimately was really good in pulling more electronic features into the mirror. I think you had very high HomeLink penetration on your RCD mirrors, other features. When you think about future generations of FDM, how is that product going to evolve? And what's the additional content opportunity maybe above and beyond this $200, $250 price point we're starting out at?

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Well, first, that's a great question. What's great about the FDM product is that it's not limited to just that technology. So whereas you're talking about a couple of hundred dollars in content for a Full Display Mirror, you can still incorporate all of our other technologies in combination with that product. And so now the concept or the ability for Gentex to sell a $400, $500 mirror, inside mirror to an OEM is absolutely realistic and it's going to happen. And I think if you look at that content, if you look at what we're doing and kind of making that mirror into an electronics module and the advantage of having an extra display in the vehicle, we think those are all point factors that are spot on with where OEMs are heading and problems they're trying to answer. So I think when you look at the overall product offering, it is a better product in terms of its global application versus anything that we've had before. And so we're excited about the long-term growth prospects.

Joseph D. Vruwink - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Associate*

And then my last question. When I think of something like HomeLink Connect, so I think you showed that for the first time, at least publicly a year ago, it's now going to be on a production vehicle this summer. So that's an 18-month turnaround ultimately. In thinking about giving 2019 revenue guidance and it's 5% to 10% growth, are some of these more recent new products, new electronic features, does that have the ability to drive that revenue growth rate, even sitting here today towards the high end or above expectations, a quicker turnaround ultimately than maybe some of your traditional products?

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Yes. When you start talking about -- HomeLink Connect, I think, is a prime example. If you're looking at Full Display Mirror, know that's a 3 year -- that's really, honestly, one of the tougher design challenges that we've ever gone through with an OEM because you're talking about packaging cameras in shark fins and rear windows, trying to find an appropriate location for a camera. It's a very difficult packaging process to go through with an OEM. When you start looking at HomeLink Connect however, this is really -- can be quicker. It's all dependent on how quickly an OEM wants to move. The issue with this is if they want to leverage the center stack, unfortunately, a lot of OEMs have a very long design cycle for center stacks. And so if it's now adding software and our technology to that area, that can be a similarly long design cycle. So we can move very quick on that side. Typically, we're working with the OEMs, trying to meet their requirements for speed. So I wouldn't look at any of products we offer and say that they would probably have the ability to impact '18 or really even '19. We're really looking at everything we showed as a 2020 and beyond revenue driver for the company.

Operator

Our next question comes from David Stratton with Great Lakes Review.

David Michael Stratton - *Great Lakes Review - Research Analyst*

Regarding the sixth OEM, can you kind of break it down what kind of content you anticipate seeing on that, whether it's mirror, camera or both?

Neil Boehm - *Gentex Corporation - VP of Engineering*

AT this point, it's mirror for sure. The camera side is still in some discussions. But we anticipate to have the full system. So mirror and camera within the next couple of months.

David Michael Stratton - *Great Lakes Review - Research Analyst*

All right. And then to touch back on the tax windfall that you're going to receive and how you look at your operating expenses going forward. Also, you mentioned your capital structure benefiting shareholders. How does this play into that overall picture when you look at how the new cash flow will be used, whether to invest harder in these new products you're bringing to market or pay down some of your debt more aggressively or even redirect it towards share repurchases? Or is there not a plan for this cash flow, and it's just going to be business as usual as you go forward?

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Well, I think if you look at it, the plan that we've been rolling out and executing the last few years has been amping up significantly how we deploy cash from our income statement. The tax change is really just an amplification of that, and we intend to continue to do the same things we've been doing the last 2 years just at a faster pace. And you could assume proportionate with the tax savings as it relates to a percentage in a net income basis.

Operator

Our next question comes from John Murphy with Bank of America.

Aileen Elizabeth Smith - *BofA Merrill Lynch, Research Division - Analyst*

This is Aileen Smith on for John. When looking at the breakout of your mirror shipments for 4Q, is there any particular reason why 4Q exterior mirrors for your international business were up so substantially year-over-year and North America down especially when comparing 4Q to the full year trend? Was there something from a launch or a timing perspective that drove that in the quarter?

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Well, there's a lot been happening in the launch side in our international markets both on inside and outside mirrors. And so that's one of the things that we like to point out as a strength of the company as the long -- for a long time, the bare case has been that mirrors themselves are dead. But really, when you look at it, you'll see a strong growth trend for us in our foreign markets where our total take rates or penetration rates have been far lower than they have been in North America. Obviously, what the battle in North America is, is that we do have higher penetration take rates. And so we're much more suspect to -- or move with what's happening in the industry at that point. In the North American side, you'll notice that it was -- outside mirrors were down slightly. There was one OEM in particular that had some take rate adjustments that affected the quarter. We're hoping to get some of that reversed on a go-forward basis, but it did have a negative impact on our growth rate in North America.

Aileen Elizabeth Smith - *BofA Merrill Lynch, Research Division - Analyst*

And have you guys broken out what your take rates are in the international business versus the North American business, whether it's for interior versus exterior mirrors?

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Well, when we look at it, we've historically talked about inside mirrors as the primary driver just to help people understand kind of what penetration story looks like in each of the regions. So in North America, we're probably in the 50% to 60% range. Currently, in the European market, we're probably in the 35% to 40% range for inside mirrors. And then in the Asian markets, we're typically in the 10% to probably maybe above 15% this year. We haven't looked at the actual penetration rate for Asia yet, but I would say it's probably in that range.

Aileen Elizabeth Smith - *BofA Merrill Lynch, Research Division - Analyst*

Okay, great. That's helpful. And then this is the second or third quarter we've now heard from you that gross margin pressure was driven by customer price reductions not offset by purchasing cost reductions. And as I understand, your price downs from your customers are typically most acute in the front half of the year. But are you seeing pricing pressure from your customers intensifying especially as volumes across some of your major regions start to flatten out and potentially decline? Or was it really just your ability to pass on some of your own price downs to your customers, getting more challenging with the supply shortages and commodity costs you cited?

Kevin C. Nash - *Gentex Corporation - CAO and VP of Accounting*

Yes. Thanks, Aileen. I think really, if you go back to really Q1, we really talked about how good the performance was in 2016, meaning our APRs that we gave back to customers were on the low end. And our PPV, our purchasing cost reductions in 2016 were at the high end. And so we had a much less of a squeeze on the margin last year. In 2017, it was the opposite of that. So APR slightly higher, primarily due to new contracts and things like that and timing of contracts and new awards. But then on the purchasing side, the commodity squeeze that we've been mentioning all year. So it's really been a year-over-year comparison. What we were pleased to see is the sequential improvement from really the first half of the year to the second half of the year. And like Steve mentioned, really going into '18, we have a little bit of more of the supply constraints or the commodity tightness in pricing, less pricing that we're getting back from the supply side. But other than that, it's really business as usual. The customers, they want all that you can give and then some. So it's our job to continue to monitor that and get something in return for that on a go-forward basis.

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Well, historically, what's been a bullish indicator for the company in terms of long-term growth prospects is when we do tend to run at a slightly higher end of our range for APRs. That's typically a bullish indicator that we have future growth prospects because we're typically negotiating contracts for 2, 3, 4 or 5 years out that include more higher-end additional content.

Aileen Elizabeth Smith - *BofA Merrill Lynch, Research Division - Analyst*

Great, that's very helpful. And then one quick housekeeping item. The $4.4 million in cost for the CEO payout, were there any tax implications off the back of that? Or is it $4.4 million both pre- and post-tax?

Kevin C. Nash - *Gentex Corporation - CAO and VP of Accounting*

With the tax changes, some of that was a lump sum, some of it, forward going. So as with the new tax law, some of that is not deductible but a good portion of it is still, so it's not material from that perspective in the overall rate.

Operator

(Operator Instructions) Our next question comes from Steve Dyer with Craig-Hallum Capital.

Ryan Ronald Sigdahl - *Craig-Hallum Capital Group LLC, Research Division - Associate Analyst*

Ryan on for Steve. Thanks for the color on OpEx guidance in 2018. But then as we look out further, is this kind of a new run rate for OpEx growth versus historically kind of that high-single-digit range?

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

No, if you look at -- no, I think the better indicator is what we're trying to do longer-term is manage OpEx expense growth at about the same rate as revenue growth rates. And so sometimes there's a timing issue of that. Leading indicator typically would be OpEx expense slightly ahead of revenue growth, but we try to match those up as closely as possible.

Ryan Ronald Sigdahl - *Craig-Hallum Capital Group LLC, Research Division - Associate Analyst*

Great. And then average ASPs have declined the last couple of years. But with several new FDM awards, and you guys mentioned that you think that will drive kind of revenue growth more on the unit side. Do you expect that to kind of inflect positively here in Q1, Q2? Or is that kind of later in the year as those awards ramp?

Steven R. Downing - *Gentex Corporation - President, CEO, Interim CFO & Treasurer*

Well, we think that if you look at the net business or the gross business, it absolutely has impacted ASPs positively. The thing we have to remember is what we're starting to grow through right now and we'll be going through for the next few years is the Mobileye runoff. So as that Mobileye content leaves the mirror over the next -- starting now and over the next several years, that's a pretty significant offset to ASPs. And so those 2 factors are going to have a roughly pretty similar kind of offsetting perspective on each other. So we really wouldn't expect it to ramp up that ASP over the next several years but really help stabilize it. The other thing that's important to note and one of the things that we like to talk about and will drive home one last time today is the inside and outside base mirror growth that we're seeing in these markets has a negative impact on ASPs but that is a bullish indicator of the company's penetration, growth story and relevance of our products and relevance of mirrors in general longer term.

Ryan Ronald Sigdahl - *Craig-Hallum Capital Group LLC, Research Division - Associate Analyst*

Great. And then last one for me, just a housekeeping item. I might have missed it earlier, but what was the short-term debt balance as of December 31?

Kevin C. Nash - *Gentex Corporation - CAO and VP of Accounting*

It's $78 million. I didn't disclose it. But yes, $78 million as of year-end.

Operator

I am showing no further questions at this time. I would now like to turn the call back to Mr. O'Berski for any further remarks.

Josh O'Berski

Thank you. Thank you, everyone, for your time and questions. This concludes our call. Have a great weekend.

Operator

Ladies and gentlemen, thank you for your participation in today's conference. This concludes this program. You may all disconnect. Everyone, have a great day.