

Latham Group, Inc.

First Quarter 2024 Earnings Conference Call

Tuesday, May 07, 2024, 4:30 PM Eastern

CORPORATE PARTICIPANTS

Scott Rajeski - *President, Chief Executive Officer*

Oliver Gloe - *Chief Financial Officer*

Casey Kotary - *Investor Relations Representative*

PRESENTATION

Operator

Good afternoon, and welcome to the Latham Group First Quarter 2024 Earnings Conference Call. All participants will be in listen-only mode. Should you need assistance, please signal a conference specialist by pressing the "*" key followed by "0." After today's remarks, there will be an opportunity to ask questions. To ask a question, you may press "*" then "1" on your touchtone phone. To withdraw your question, please press "*" then "2." Please note, this event is being recorded.

I would now like to turn the conference over to Casey Kotary, Investor Relations Representative. Please go ahead.

Casey Kotary

Thank you. This afternoon, we issued our first quarter 2024 earnings press release, which is available on the Investor Relations portion of our website, where you can also find the slide presentation that accompanies our prepared remarks.

On today's call are Latham's President and CEO, Scott Rajeski; and CFO, Oliver Gloe. Following their remarks, we will open the call to questions.

During this call, the company may make certain statements that constitute forward-looking statements which reflect the company's views with respect to future events and financial performance as of today or the date specified.

Actual events and results may differ materially from those contemplated by such forward-looking statements due to risks and other factors that are set forth in the company's annual report on Form 10-K and subsequent reports filed or furnished with the SEC, as well as today's earnings release. The company expressly disclaims any obligation to update any forward-looking statements, except as required by applicable law.

In addition, during today's call, the company will discuss certain non-GAAP financial measures. Reconciliations of the directly comparable GAAP measures to these non-GAAP measures can be found in the slide presentation that accompanies our prepared remarks, which can be found on our Investor Relations website.

I'll now turn the call over to Scott Rajeski.

Scott Rajeski

Thank you, Casey. Good afternoon, everyone, and thank you all for joining today's call to review our first quarter 2024 results and discuss our latest business trends.

In terms of key takeaways, first, we were pleased with our first quarter results. They represented a solid start to the year and exceeded the guidance we provided at the time of our fourth quarter conference call in March.

Second, our performance demonstrated our ability to execute effectively during periods of uneven order flows and reflects the benefits of our reduced cost structure and actions we have taken to accelerate our value engineering efforts and lean manufacturing initiatives. These actions continue to drive ongoing production efficiencies and incremental capacity in our plants, providing us with more flexibility to serve customers with our industry-leading lead times; and

third, we continue to maintain a substantial cash position even after the usual seasonal outlay for working capital and an \$18.8 million debt repayment. This cash provides Latham the significant resilience to manage through soft business conditions for the pool industry and the resources to take advantage of opportunities to drive future growth.

Taking a closer look at Q1, after a slow start to the quarter, we saw a significant pick-up in orders starting in mid-March. Our operations team was able to do a great job on execution, achieving lead times of 3 to 5 days. Fiberglass pool sales, while down year-on-year, showed relative strength and continued to represent the majority of our in-ground pool sales.

On our last earnings conference call, we cited Latham's priorities for 2024. The first was to continue to drive the adoption and awareness of both fiberglass and automatic safety covers, and in the first quarter, we made considerable progress in the areas of new and refreshed product introductions as well as new dealer wins.

During the quarter we launched the Enchantment plunge pool series through our California plant, which serves the important California, Arizona, and Nevada markets. Plunge pools are becoming increasingly popular as they provide the homeowner with space-saving, lower-cost options that are ideal for aquatic exercises and rehabilitation. In the first quarter, we also re-launched the Providence and Tuscan series in North America, which is a very trendy rectangular pool with an attractive side-entry feature. Additionally, we put the finishing touches on a new fiberglass pool model that has a broad array of features, including swim-up seating and a built-in spa that is currently available to our largest dealers. We are also in the early stages of rolling out a line of plunge pools in our vinyl liner in-ground pool category. More on that in the coming months.

With respect to automatic safety covers, which are another key priority for us, we continued to work with our pool cover distribution network as well as many of our competitors' dealers, including concrete pool builders, to advance awareness and adoption of these products. In addition to providing unparalleled protection, these autocovers offer significant resource savings, resulting in up to a 70% reduction in both pool heating costs and chemical usage. We are continuing to drive operational improvements in our autocover plants to reduce lead times and gain incremental capacity. Our operations team is also working on changes to our product lineup that will expand price points and capabilities. And, we're making it a key focus to ensure that all of our newly launched pool models in our in-ground category are autocover-ready.

We also continued the successful roll-out of Measure by Latham, the first tool of its kind that simplifies the pool measurement and quoting process for liner and cover installers. This easy-to-use AI-powered device provides dealers with high-performance measuring accuracy with precise specifications for swimming pool covers and vinyl liners—all within minutes and all integrated with our project management portal which enables dealers to quickly and easily receive quotes and submit and track orders. As you can imagine, this tool has been met with a very positive response from our dealers and contractors. We will continue its roll-out to make sure all our dealers have it and all the functionality is in place ahead of the 2025 pool building season.

Latham's extensive and appealing product line-up, together with our industry-leading service levels and best-in-class lead times, are strengthening our ability to attract new dealers. In the first quarter, we were able to convert several new dealers in the U.S. and Canada that we believe will enable us to continue to drive penetration and growth in several key markets. For some of these dealers, while they are established pool builders, this will be their first experience

with fiberglass products. They are motivated by the much shorter installation time, which is of course very attractive to their end consumers, as well as the ease of installation and the aesthetics of the product, both of which often result in additional leads for them from neighboring homeowners. In working with Latham, even the most experienced new dealers go through our bootcamp to be trained in fiberglass installation to maximize their success.

The second priority for 2024 that we mentioned on our last earnings call is our programs to continue to gain additional operating efficiencies through value engineering and lean manufacturing initiatives. These structural cost benefits will have a long-term positive impact on Latham's margin profile and will be an important factor for us in 2025, when we expect improved market conditions to drive increased volumes. For example, the initial benefits from these programs in our largest liner and cover manufacturing plant include an 8% improvement in labor efficiency, a 20% increase in throughput and an overall improvement in employee health and safety. All of this contributed to our first quarter margin performance.

Lastly, we prioritized maintaining a strong balance sheet to both retain our resilience in today's soft market environment and retain the resources to support future growth. Oliver will provide details on that in a moment, but I can say that we have been very disciplined in our spending and have the operational and financial flexibility to flex up and down in response to market conditions as well as take advantage of opportunities to drive future growth.

With that, I will turn over the call to our CFO, Oliver Gloe, for a first quarter financial review. Oliver?

Oliver Gloe

Thank you, Scott, and good afternoon, everyone.

Please note that all comparisons that I will discuss today are on a year-over-year basis compared to the first quarter of fiscal 2023, unless otherwise noted.

Our first quarter results exceeded our expectations, reflecting strong execution, cost savings and our lean and value engineering initiatives. As we anticipated, first quarter comparisons reflected the challenging macroeconomic conditions that have reduced pool starts. Net sales were \$110.6 million compared to \$137.7 million in Q1 of 2023, down \$27.1 million or 19.7%.

The 23.9% decline in in-ground pool sales was primarily due to lower packaged pool demand, while fiberglass pool products continued to show relative strength and continued to account for the large majority of Latham's in-ground pool sales. Liners remained more resilient, declining 9.2% due to the replacement cycle of these products and covers were down 17.9%.

We were pleased to see our gross margin increase 350 basis points to 27.7%, despite lower sales. This increase was driven by carry-over benefits from the cost reduction actions we took in 2023, as well as lower raw material costs and lean manufacturing initiatives. Year-on-year comparisons also benefitted from two meaningful headwinds impacting Q1 2023 – consuming the remainder of our high-cost inventory, and our inventory reduction programs which resulted in under-absorption at our plants. These factors more than offset the impact of lower utilization from lower volumes and wage increases.

SG&A expenses decreased to \$26.3 million, down \$6.8 million primarily due to our ongoing cost reduction efforts and a \$5.1 million decrease in non-cash stock-based compensation expense.

For 2024, non-cash stock-based compensation is expected to amount to approximately \$8 million.

Net loss was \$7.9 million, or \$0.07 per share, compared to a net loss of \$14.4 million, or \$0.13 per share, for the prior year's first quarter.

Adjusted EBITDA of \$12.3 million was up from the prior-year period by \$1.3 million or 11.4% compared to \$11.0 million in Q1 2023. This strong performance is the result of solid execution in a difficult market, primarily due to cost savings and progress made with our lean and value engineering initiatives. Adjusted EBITDA margin was 11.1%, a considerable improvement compared to 8.0% in the prior year period. As you know, our full year 2024 guidance implies decremental EBITDA margins for the remainder of 2024, primarily reflecting our planned investments in future growth. Notably, this involves continued investments in sales and marketing and engineering and R&D to accelerate conversion to fiberglass pool products, ongoing digital transformation programs, and normalized performance-based compensation.

Turning to our balance sheet, we continue to maintain a strong financial position with cash of \$43.8 million at the end of the quarter, after the repayment of \$18.8 million in debt in Q1. Net cash used in operating activities was \$34.5 million, reflecting a seasonal increase in net working capital of \$41 million as the company enters peak pool-selling season.

Total debt for the period was \$282.8 million with a net debt leverage ratio of 2.7, and our capital expenditures were \$5.3 million for the first quarter in 2024, considerably lower than the \$9.9 million in the prior year. We expect a comparable run rate in quarterly capex throughout 2024. Our cash position and capital expenditures are in line with our expectations and reflect seasonality as well as our conservative capital allocation strategy given the uncertain economic outlook. That said, we will continue to deploy our capital opportunistically to best position us for accelerated profitable growth as market conditions improve.

First quarter results, together with our current visibility, underpin the guidance metrics we provided at the time of our fourth quarter 2023 earnings release.

With that, I will turn the call back to Scott for his closing remarks.

Scott Rajeski

Thank you, Oliver.

While the first quarter represents a small percentage of our annual revenues and Adjusted EBITDA, we are very pleased with how well our teams executed amid a choppy start to the season. Latham's strong execution, cost savings and lean and value engineering initiatives all contributed to quarterly performance that exceeded our guidance and demonstrated our ability to execute efficiently. We appreciate the commitment and engagement of Latham's team members throughout our organization, who made this possible. We also want to thank all of our customers and suppliers who continue to be strong supporters of Latham.

Our first quarter results support our full year guidance expectations for 2024 and underpin our confidence in Latham's ability to effectively navigate the current market environment and emerge as an even stronger company.

Operator, I would like to open the call to questions.

QUESTION AND ANSWER

Operator

Thank you. We will now begin the question-and-answer session. To ask a question, you may press "*" then "1" on your touchtone phone. If you're using a speakerphone, please pick up your handset before pressing the keys. To withdraw your question, please press "*" then "2". In the interest of time, please limit yourself to one question and one follow-up. At this time, we'll pause momentarily to assemble our roster.

Our first question comes from Jonathan Bettenhausen from Truist. Please go ahead.

Jonathan Bettenhausen

Hey, I'm on for Keith this evening. Thanks for taking my question. On the 2024 cost savings realization, I think last quarter you indicated targeting maybe about \$4 million in incremental savings. How is that progressing? It looks like maybe most of that has already been realized here in 1Q. Am I looking at that right?

Oliver Gloe

Yes, you're absolutely right. We had about a \$4 million spill over from our cost savings initiatives. All the initiatives are fully implemented. Of that \$4 million, about \$2.7 million is in our Q1 with the remainder being left for Q2.

Jonathan Bettenhausen

Okay, got it. Were there any surprises in sales momentum heading into the second quarter? Was the demand ramp kind of about what you expected in March?

Scott Rajeski

Yes. I think if you look at how Q1 played out for us, and I think we've heard this from others, a little bit slower start from January and February right around the time we were on our Q4 earnings call. I think we saw a really nice pickup in the seasonality, maybe a few weeks jumpstart there as the season took off, as we moved through the back part of March. I think as we look moving through April here as well, I'd say the season is kind of ramping as expected on track with the guidance that we reconfirmed out there today.

Jonathan Bettenhausen

Okay, got it. Appreciate it.

Operator

Yes. The next question comes from Tim Wojs from Baird. Please go ahead.

Tim Wojs

Hey everybody. Good afternoon. Maybe just first question, Scott. In the prepared remarks you talked about seeing some incremental traction on dealer-adds. I'm just wondering if the investments that you've made and then just with the slower pool environment, if you are seeing an incremental propensity from dealers to kind of consider fiberglass and then also consider being part of the Latham network?

Scott Rajeski

Yes. I think, Tim, as we've talked over the years, part of what we've always done is constantly recruit and attract new dealers to Latham on all aspects of all product lines, really a big focus is on fiberglass. I think when you come back and just look at the value proposition of fiberglass,

the speed of the install, and then the lower cost compared to, let's say, concrete pools, I think that continues to resonate at both the dealer and homeowner level, giving them a lower-cost option, especially as we've seen the cost of the pool drastically increase at the consumer level. Then you combine that with the cost of financing, I think it's just giving them an opportunity to jump in and establish themselves as a dealer, get trained up. It's all nice incremental volume for those dealers. And again, I think we show them, look, this is a long-term play for us, right? When the market rebounds, they'll be well-positioned, they'll be trained, they'll have gone through the boot camps, and they'll be ready to rapidly increase their productivity and efficiency for fiberglass pools.

Tim Wojs

Okay. You say it's kind of more of what you've seen over time. It's not that, hey, there's a slower environment and there's any sort of increased view for fiberglass. It's just a kind of a constant share that you're kind of seeing.

Scott Rajeski

Yes. I think we will need a little clarification there, Tim. It's a good point. We've become a little bit more aggressive out there. So, you could say that the number of dealers and the quality of dealers we've been adding is much better than maybe in the last two, three, four years during the difficult supply chain challenge issues. I think why they're choosing us, well, if you look at our footprint, we have a great footprint throughout the entire country. So, we bring a lower cost-to-serve for all dealers throughout the country. If you look at the quality of our pools, and then where we stand from a lead time and service standpoint, we're in a really good position. And that's kind of back to, it was Jonathan's question, right out of the gate here. As we came through 1Q, our ability to quickly respond to incremental demand signals in March is really what enabled us to kind of post-up some really good results in 1Q.

Tim Wojs

Okay. Good. Then I guess from a seasonality perspective, from a sequencing perspective, should revenue be the highest in Q2 and then lower a little bit in Q3 and then see a drop off in Q4? Would that kind of be how profitability would also phase through the year, just trying to think about how to think about the seasonality impact? We haven't seen I guess normal seasonality in three or four years.

Scott Rajeski

Yes. So, Tim, fair question. When I was driving in this morning, I was thinking about, I've been in the business for 14 years. I don't think I've seen a normal season in 14 years. I'm not really sure what a normal season is anymore with everything out there. But I'd say we're kind of returning to what has been more typical of the seasonality we've seen. We've talked over the years, you could probably argue, think of a 50-50 split, right? 1Q came in just a little over 20%. Clearly 2Q and 3Q is the bulk of the season. So, I think if we just said around 30%-ish in 2Q and 3Q ballpark, give or take a few rounds, then the balance coming in 4Q, and then I will let Oliver address it, but you can probably argue that the EBITDA profile would be a little similar to that, you know. But again, we had the decremental conversation on the last call. So, you've just got to watch that as we move through the rest of the year, but again, we are kind of happy with how the season is ramping. I think it's lining up really nice to our guidance and overall market expectation. Oliver, do you want to talk about the profitability profile that flows through?

Oliver Gloe

You know, from an EBITDA cadence, if you take our mid-point guidance, I think right now it's \$65 million, deduct our first quarter contribution from that, you're left with about \$52.7 million, right? Now, think of that being by majority contributed by Q2, Q3. Those quarters are by far the quarters with the most sales activity and EBITDA contributions, with a small share in Q4.

Tim Wojs

Okay. That's helpful. Thanks everybody.

Oliver Gloe

Welcome.

Operator

The next question comes from Andrew Carter from Stifel. Please go ahead.

Andrew Carter

Hey, thanks. I just wanted to ask, kind of late in the quarter, what led to the outperformance. And, you said shipments picked up, I know you hate to talk about it but, Pool Corp called out the weather – obviously hit the south, hit the northeast where you're strong. In addition, again, I know something you hate to talk about, but, kind of, the channel inventory: did you see anything like a difference between your shipments and what you think went out of the channel? Particularly, I guess, for the package pools, as well as the covers? Thanks.

Scott Rajeski

So, hey Andrew. Good question there. I think as we looked at it, in-ground liners, right? Was really a key point for us in Q1 as that season started the ramp in the south, slowly moving up to the north? And again, if we kind of look at the regional differences, you are right, the northeast is a little bit tougher, wetter, a little bit colder start to the season. But in the warmer climates where it really starts to take off for us, we are sitting, in some cases in a few of the plants, with one-, two-day lead times for liners. As those orders started to flow, we were able to convert those in a two- or three-day cycle and really take advantage of the push we saw there and I think the other really strong point for us was fiberglass, right? Fiberglass performed extremely well. We have inventory on the ground and the common models in a lot of territories. Those orders were rolling in and let's say where the weather was more favorable, we were able to get pools pushed out to dealers, get them in the ground. So, good execution across the board by both the operations team and our customers there. Fiberglass is still making up the majority of the in-ground category. I think that part has continued to be a little bit slow for us. You know, we've really not seen the restocking or pull-through orders from the distribution branches, whether it's Pool Corp or any of our other big distribution partners, Heritage, et cetera out there. I think that's what we'll start to see as we move through 2Q, and product really starts to move off the shelf as we hit the peak pool building season here in May, June, and July.

Andrew Carter

Second question. Looking, kind of, at your SG&A, and granted, who knows, my math could be wrong, but it looks like for the final nine months of the year, I've got SG&A up \$31 million to \$33 million. That's excluding charges, also excluding SBC. You were flat. Could you dimensionalize that, kind of, increase over the final nine? I know, there are some incentive

comp restorations in there that you can't avoid. There is not really any cost savings in there but there is some also variable investments, as you say, get ready when starts accelerate. And how much is that truly variable and could you quickly pull that back and when would you know whether you wanted to pull that back or not and at what point the season? Thanks.

Scott Rajeski

Yes, I will hit the last part Andrew. First, you know, when would we feel the pullback /anything on the variable portion of the spend there. We typically, kind of, wait until we get into late-May or mid-June, which will really give us a read for how the season is playing out in terms of pool starts. Is that in line with our expectations or anything? So, you know, we are in that waiting game of peak build where we don't want to start doing anything too drastic, too early. But we've also talked about how we have made incremental investments. We are trying to retain folks. We are trying to push leads out there to dealers with our sales and marketing efforts. So, we don't want to pull the trigger too quickly. But again, there is peak that's variable in there that if we had to toggle, if the market worsened more than what our expectations – and I think that's the key point, right – our outlook for the market was probably further down than others in the industry and we think we are tracking to that, roughly-15% down in new pool starts versus last year's number. So, we've got many levers we can pull there. Oliver, do you want to address the first part of the question?

Oliver Gloe

Yes absolutely. You know, two drivers that increase SG&A year-over-year. We talked about this net of performance-based compensation that is about \$7 to 8 million, and then Scott mentioned the investments into future growth to over proportionately participate once the market comes back. So, those are really the two drivers there for SG&A.

Andrew Carter

Thanks. I will pass it on.

Oliver Gloe

Thanks Andrew.

Operator

The next question comes from Shaun Calnan from Bank of America. Please go ahead.

Shaun Calnan

Hey, guys. Thank you for taking my question. Just given the sales beat in the quarter and talking about the pickup as we, kind of, went through the quarter and through March, is there any reason you guys chose not to raise the guidance? I am just curious if there is maybe a pull-forward in demand or...it doesn't sound like it, but if you are starting as the orders slow in April versus your original expectation?

Scott Rajeski

I think you could chalk it up, Shaun, probably, partly, just to timing, how we had the quarters profiled out. We had an expectation of what total market was going to do. You know, I think as we tried to work back through what does the normal season look like. We probably took a little bit more of a conservative approach in Q1, assumed a little bit of a slower start. Again, we had the luxury at that point in time of seeing how January and February was playing out where

we did the quarter, and look, you know, we did see a nice ramp up of orders in March. I don't believe any of it was pull-forward demand. I think it was just, weather was good in some markets, that helped us. We were in a good position from a lead-time ability to quickly turn those short-cycle orders and I think when we look out there and talk to dealers and others in the industry, I still believe our view of the market being down 15% overall still feels about right. Look, we've only completed roughly a little over 20% of the year for us. We've really got to move through this big quarter here, 2Q, see how the season ramps, fight through the weather. As I mentioned up top, five weeks into the quarter, so far I'd say things are tracking extremely well, tracking towards what our guide and projections are and I think we've got to get through 2Q here and when we chat in August, that's when I think we'll be able to take a full assessment of what we think the full year is going to look like.

Shaun Calnan

Okay, got it. And then, do you have any early metrics on the Measure tool in terms of adoption by dealers or revenue at this point?

Scott Rajeski

Yes, it's just rolling out there for covers, right? And if you if you think about it, the cover season really kicks in for us in the fall, so it's a mass push of getting all the units out there deployed into the field with the dealers, with the view as they're out there opening pools for the season, right? They're evaluating the covers on the pools, we're encouraging them to measure the covers, inspect them, do they need a replacement? Take those measurements now while they're out there, get trained up here, get geared up. Look, this is a big deploy for us in terms of units out there and the training, we're still in the beta testing of what we're doing. The liners, again, early good success on that, so we're also teaching them how they could be measuring for liners and as we get ready to do that launch in the fall for the early 2025 season. But we're not at a point where it's of any significance that we want to be talking about, metrics, units, number of units in dealers hands, number of units we're processing.

We are taking orders, we are processing orders through our plants, shipping them back out to dealers, and I think the key thing here is response rate acceptance has been phenomenal, and I think we'll eventually be able to talk about market share gains we're going to be able to achieve, again, by attracting dealers who may have been buying from other manufacturers out there coming to Latham, because this is a huge productivity and time-saving device for them. And also ensuring the accuracy of those measurements that they're taking, almost fool-proofing the quality of the liner and cover they're going to get because they will know the measurements are dead-on based on the AI and intel in the device as it moves through the system. So, we're really excited about it, I think this will be game-breaking for us and as we move through the next couple of quarters we'll start disclosing more information on units deployed, number of dealers, and volumes and stuff, processing through. It's just a little too early to get out there with that that data yet.

Shaun Calnan

Great, thank you.

Scott Rajeski

Welcome Shaun.

Operator

Again, if you have a question, please press "*" then "1", the next question comes from Matthew Bouley from Barclays. Please go ahead.

Anita Dholakia

Good evening. You have Anika Dholakia here on for Matt, thanks for taking my questions. The first question is on kind of your customer base. So, we've seen some industry peers have spoken to more challenged demand for their lower-end pools and I'm just curious if you're seeing similar mix effects and maybe how you think this could trend into the second half given the current macro backdrop? Thanks.

Scott Rajeski

Yes, so similar views and again, there's two sides to this coin – one that really helps us and one that's a drag. But, again, this was all contemplated in the guide we issued and the reconfirm, right? For fiberglass we're seeing really good performance because it's a lower-cost option versus concrete pools. So as consumers are trading down from the concrete price points, they're stepping into fiberglass pools which are working really well for us in a \$75K to \$100K consumer price point. The package pool or the other piece of the in-ground vinyl business is doing okay, but that's more of the middle America, that's where a lot of the pool financing occurs that's out there. I think we're trending to the numbers we had expected in our guide overall, but what's happening is we're seeing good traction with our Radiant panels and Radiant pools because that's a lower-priced in-ground vinyl-liner option for those consumers that – I hate to say "stepped down to" because the Radiant panel and pool is a really, really nice pool compared to the other options out there at that are more entry-level or second-level pools that you'd be stepping into versus your typical on-ground or above-ground pool. So, a little bit of a mixed bag, but when we look at the fiberglass, that's what we like to see, we like to see the traction we're getting with the Radiant pool out there and the acceptance as well.

Anita Dholakia

That's really helpful, thanks. And then second just curious how are you guys thinking about current capacity levels today? Should we assume that there's going to be additional capacity investment in the near term, or maybe given your Kingston investment, some other cost initiatives, maybe you're holding off on that? Thanks.

Scott Rajeski

Yes, so on the on the capacity side, we really like where we sit with capacity today from all the investments, getting Kingston brought online, and just thinking about Kingston, right? It gives us the opportunity to attract new dealers to those locations, right? They now have capacity in their backyard with fiberglass, much more capacity than we had before. They're looking at Latham as a manufacturer of choice. It gives them a lower-cost model to pass on to their consumers, with more demand. So we had really, really nice customer-wins up there. I think we might have briefly touched on that in the last call. Similarly, in other areas of the market, we've got good capacity and that leads to great service levels and lead times. Where we will continue to invest is in product launches, product lineup, new models, new feature-rich fiberglass pools. We talked a lot about the plunge pool series and some of the new models we're getting out there where consumers are looking for particular features whether it's a side entry, bigger tanning ledges, or some of these smaller cocktail/plunge pools. So, I think it's those types of investments. But look, the operations team continues to drive a lot of really, really good value

engineering and lean events in the facilities, which is actually creating more capacity. And, not to sound like a broken record, but, if you go back to the big cost reduction initiatives we were able to do last year, taking five facilities or locations offline, it's because of all those efforts of the operations team is freeing up capacity. So, we're in a good position. As of right now it's not like we need to go do chunky-type of capacity, it's tweaks in each of the small facilities to make sure we are well positioned looking out to the '25, '26, '27 market where new pool starts will be.

Anita Glock

Great. Thank you, guys. Good luck.

Scott Rajeski

Welcome, thank you.

Operator

The next question comes from Susan Maklari from Goldman Sachs. Please go ahead.

Susan Maklari

Thank you. Good afternoon everyone. My first question is, you know, thinking just a little bit about the input cost, the environment, how that came together through the quarter, any changes that you are seeing as you think about the balance of the year? Perhaps any chemicals that are coming up or those types of things? And then, just any thoughts on price cost, how that trended through the quarter and the outlook there?

Oliver Gloe

Yes, let me take that, Susan. So, let me start with our annual guidance and then I'll go back and take that back to Q1. So, we guided on the price flattish, and on deflation, we added some modest deflation to our guide, and in Q1, we have seen deflations in several parts of our baskets, primarily resins, PVC film, aluminum, quite in line with our guide and our expectations, maybe a little bit better, more favorable. But we are also seeing some increases most recently driven by styrene and benzene. So, I would say overall our guidance being a modest deflation for the year, it's quite intact and confirmed by our Q1 performance. I will give you a similar comment on the pricing side. We generally see prices sticking. In our last earnings call we said that some of our product categories we took down a little bit. Some we took up a little bit, but overall, we guided towards a flattish price and, again, the same is true for Q1. We saw flat pricing in Q1.

Susan Maklari

Okay. All right. That's helpful. And then, you know, we kind of just look across our coverage, I think there are some companies that have talked about seeing perhaps a moderation in activity as rates have moved higher in the last couple of weeks or so. It doesn't sound like you are seeing that as we get into the kind of core of the pool season, but I guess Scott, can you just talk a bit about what you are hearing on the ground from some of your dealers? Has there been any response to the moving rates and just how are you thinking about that as we are getting into the spring and the summer?

Scott Rajeski

Yes. So, Susan again if we go back to kind of our guide for the year, right? We were expecting pool starts to be down further than others and probably the rest of the entire industry. I think some of the commentary we have seen out there is that people are experiencing closer to our number of around 15% down for new pool starts. There is really not a lot of financing activity out there right now. So, as rates continue to trend up, trend down, bounce where they are, at this point, I don't really think that's impacting our dealers, our consumer base. We typically have the higher-end of the market, more of the cash buyers. We are actually seeing the \$75-100K+-type pool backyards holding up extremely well. As those individuals have the capital that they can deploy to make the pool purchase.

So, I think all helpful to us as we go forward here, I think we are in a good position there, Susan. We are all looking forward to when the Fed starts to see the rate go down. So, I think that will really start to allow others to come back into the market. We got some new intel from one of our third-party financing companies. I think they have tightened up the credit limits and I think what they are doing now is they are getting a little bit creative. One of our partners has now introduced the 20-year loan again. They had pulled that back over the last year or two. So, the fact that now you can go out there and finance a pool project for 20 years helps lower the overall monthly payment for a consumer which is keeping folks out there. And I think dealers are also getting very creative at scaling back the overall dream of the homeowner for the backyard, right?

Homeowners are coming in, they have got their pool, their huge patios, their outdoor kitchen, the fire pit, the pavilion, all the lighting, and the landscaping, and I think dealers are saying, "Hey, look, we'll quote out the full backyard project for you, but we're going to do it in segments. If you can only afford X, let's get the pool in and let's get your 3 feet of concrete in. We can fit you into your budget and payment that way. And then we will come back in a year or so and finish up your dream of what you want your whole backyard to look like with a bigger patio, getting that fire put in there, and the outdoor kitchen.

So, I think it's people being creative. In some cases, dealers have had to lower their price to the consumer as they readjust their pricing model in a lower-demand and lower-new-pool-start environment. So, it's really, I'd say, accumulation of several different factors, they are working on out there, Susan, to try to keep business flow and keep their employees engaged out there. Well, we're – I hate to say it – we're looking forward to getting into '25. We still think '24 will be the trough. New pool starts, I don't see how they could be any worse next year than they are this year. They should go up, barring any unforeseen incident. But that's where we want to be conservative in our actions at the Company here. Making sure we have got the capacity, we have got the investments in plants and personnel. We keep investing in new models, and new product launches because we are looking forward to '25 and '26 when the market rebounds.

Susan Maklari

Okay. That's very helpful color, Scott. Thanks for that and good luck with everything.

Scott Rajeski

Thanks Susan. You're welcome.

Operator

There are no more questions in the queue, and this concludes our question-and-answer session. I would like to turn the conference back over to Scott Rajeski for any closing remarks.

CONCLUSION**Scott Rajeski**

Yes, well, thanks everyone for participating in this afternoon's call. Look forward to seeing you all at upcoming conferences, in meetings, and I hope everyone has a good evening and everyone have a safe summer until the next time we talk. Take care.