25-Jul-2024

Masco Corp. (MAS)

Q2 2024 Earnings Call

CORPORATE PARTICIPANTS

Robin L. Zondervan
Vice President, Chief Accounting Officer and Investor Relations/FP&A, Masco Corp.

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

Richard Westenberg
Vice President, Chief Financial Officer and Treasurer, Masco Corp.

OTHER PARTICIPANTS

Matthew Bouley
Analyst, Barclays Capital, Inc.

Stephen S. Kim
Analyst, Evercore ISI

John Lovallo
Analyst, UBS Securities LLC

Adam Baumgarten
Analyst, Zelman & Associates

Anthony James Pettinari
Analyst, Citigroup Global Markets, Inc.

Sam Reid
Analyst, Wells Fargo Securities LLC

Susan Maklari
Analyst, Goldman Sachs & Co. LLC

MANAGEMENT DISCUSSION SECTION

Operator: Good morning, ladies and gentlemen. Welcome to Masco Corporation's Second Quarter Conference Call. My name is Ludie and I will be your operator for today's call. As a reminder, today's conference call is being recorded for replay purposes. [Operator Instructions]

I will now turn the call over to Robin Zondervan, Vice President, Investor Relations and FP&A of Masco Corp. You may begin.

Robin L. Zondervan
Vice President, Chief Accounting Officer and Investor Relations/FP&A, Masco Corp.

Thank you, operator, and good morning everyone. Welcome to Masco Corporation's 2024 second quarter conference call. With me today are Keith Allman, President and CEO of Masco; and Rick Westenberg, Masco's Vice President and Chief Financial Officer.

Our second quarter earnings release and the presentation slides are available on our website under Investor Relations. Following our remarks, we will open the call for analyst questions. Please limit yourself to one question, with one follow-up. If we can't take your question now, please call me directly at 313-792-5500.

Our statements today will include our views about our future performance, which constitute forward-looking statements. These statements are subject to risks and uncertainties that could cause our actual results to differ materially from the forward-looking statements. We've described these risks and uncertainties in our risk factors and other disclosures in our Form 10-K and our Form 10-Q that we filed with the Securities and Exchange Commission.

Our statements will also include non-GAAP financial metrics. Our references to operating profit and earnings per share will be as adjusted unless otherwise noted. We reconcile these adjusted metrics to GAAP in our earnings release and presentation slides, which are available on our website under Investor Relations.

With that, I will now turn the call over to Keith.

Keith J. Allman

President, Chief Executive Officer & Director, Masco Corp.

Thank you, Robin. Good morning, everyone, and thank you for joining us today. As we sit here midway through the year, I'm pleased with our performance. Despite a challenging macroeconomic environment, we have delivered solid financial results with our continued focus on operational excellence, brand, service and innovation. Additionally, the strength of our repair and remodel oriented product portfolio has enabled us to drive operating profit margin expansion in the first half of the year, better than we expected, despite a decrease in sales.

Turning to our second quarter results. Please refer to slide 5. Demand continued to stabilize as net sales decreased 2%, in line with the prior two quarters. Second quarter sales performance was primarily impacted by lower volume and mix. In the quarter, our gross profit grew $16 million and gross margin rose 140 basis points to 37.6% as a result of our ongoing initiatives to drive operational efficiencies and achieve cost savings. Our solid execution resulted in operating profit of $399 million, and operating profit margin of 19.1%. In addition, our earnings per share grew 1% to $1.20 per share.

Moving to our segments. Plumbing sales increased 2% overall and 1% excluding the impacts of acquisitions and currency. In local currency, North American Plumbing sales increased 5% overall, and 2% excluding the impact of acquisitions. In International Plumbing, sales decreased 1% in local currency, demonstrating continued signs of stabilization, particularly in Europe and China.

Operating profit for the segment was up $4 million to $249 million, and operating margin was 19.9%, largely in line with the prior year, driven by our pricing discipline and operational performance, as we continue to focus on productivity, efficiency cost savings. We are pleased with our performance in the Plumbing segment throughout the first half of the year, as our teams both in North America and International, continue to leverage our operating system and execute on our strategic priorities. Lastly, in Plumbing, Delta Faucet was awarded the J.D. Power Customer Service distinction for the third year in a row. This award recognizes our outstanding customer service and reinforces our commitment to industry-leading service.

Moving to our Decorative Architectural segment. Sales decreased 7% in the quarter. Overall, paint sales were down high-single digits, as DIY paint sales decreased low-double digits, while PRO paint sales grew mid-single digits. In PRO paint, we continue to execute on our strategic initiatives to grow share with our partner, the Home Depot. Our partnership dates back over 40 years, and together, we are focused on meeting the needs of our customers through quality, service, brand and performance. We are proud of sales growth and market expansion with the PRO painter, and we are continuing to invest to drive additional growth going forward.

Operating profit for the segment decreased $6 million to $174 million, while operating margin was up 80 basis points to 20.8%. For the first half of this year, demand in our Decorative segment overall was generally in line with our expectations. However, DIY paint was more challenged than expected, partially offset by stronger performance in PRO paint.

Turning to capital allocation. We continue to generate strong free cash flow during the quarter and maintained a solid balance sheet. As a result, we executed on our capital deployment strategy and returned $206 million to shareholders through dividends and share repurchases.

Now, for a few comments on our outlook for 2024. Overall, sales for the total company were largely in line with our expectations for the first half of the year at down low-single digits. As uncertainty within the broader macroeconomic environment has continued, we are tempering our expectations for sales in the second half of the year from up low-single digits to roughly flat, leaving our full year sales within our previously guided range of plus or minus low-single digits. However, we are raising our full year operating margin expectation to be within the range of 17% to 17.5%, driven by the strong first half performance in the Plumbing segment.

We remain confident in our ability to drive margin expansion through our continued execution of our operating system. Additionally, with our strong focus on our cost structure and productivity, we are well positioned to leverage volume growth when the market returns to normalized growth rates. We now anticipate adjusted earnings per share for 2024 to be in the range of $4.05 to $4.20 per share, narrowed from our previous expectations of $4 to $4.25 per share.

We continue to believe that the long-term fundamentals of our repair and remodel markets are strong and that structural factors, such as age of housing stock, consumers staying in their homes longer, and higher home equity levels will drive increased repair and remodel activity in the mid to long-term.

With these favorable fundamentals, the continued successful execution of our strategic initiatives and our disciplined capital deployment, we are well positioned to drive shareholder value creation. We will continue to invest in our brands, capabilities and people to outperform the competition and deliver double-digit EPS growth through cycles for our investors.

Now, I'll turn the call over to Rick to go over our second quarter results and 2024 outlook in more detail. Rick?

Richard Westenberg

Vice President, Chief Financial Officer and Treasurer, Masco Corp.

Thank you, Keith, and good morning, everyone. Thank you for joining. As Robin mentioned, my comments today will focus on adjusted performance excluding the impact of rationalization charges and other onetime items.

Turning to slide 7. Sales in the quarter decreased 2% year-over-year or 1% excluding the unfavorable impact of currency. Our acquisition of Sauna360 in the third quarter of last year added 1% of growth to our second quarter results.

In local currency, North American sales decreased 1% or 2% excluding acquisitions. In local currency, international sales decreased 1%. Despite modestly lower sales level, our initiatives to drive operational efficiencies and our favorable price/cost performance in the quarter contributed to significant gross margin expansion of 140 basis points to 37.6%. SG&A as a percent of sales was 18.5% and was impacted by higher employee related costs.

Overall, our operating profit was $399 million in the quarter, down slightly year-over-year, driven by lower sales. However, our margin remained strong at 19.1%. Our strong margin performance was primarily driven by cost savings initiatives and a favorable price/cost relationship. We also grew EPS during the quarter by 1% to $1.20 per share.

Turning to slide 8. Plumbing sales increased 2% in the quarter or 3% excluding the unfavorable impact of currency. Volume in our Plumbing segment was flat year-over-year for the first time since the second quarter of 2022, demonstrating encouraging signs of stabilization. Pricing actions increased sales by 2% and acquisitions contributed another 2% to growth year-over-year. This was partially offset by unfavorable mix and currency, which reduced sales by 1% each.

North American Plumbing sales increased 5%, including 3% related to acquisitions. Delta Faucet delivered another quarter of low single-digit sales growth and our Watkins Wellness spa business returned to year-over-year sales growth before factoring in the benefit of the Sauna360 acquisition. In local currency, International Plumbing sales decreased 1%, driven by unfavorable mix, partially offset by pricing actions and favorable volume as we continue to see signs of stabilization in our key markets of Europe and China.

Segment operating profit in the second quarter was up $4 million or 2% year-over-year, and operating margin was 19.9%, in line with the prior year. This operating profit performance was driven primarily by cost savings initiatives and a favorable price/cost relationship, partially offset by unfavorable mix and higher employee-related costs.

Turning to slide 9. Decorative Architectural sales decreased 7% for the second quarter. In the quarter, total paint sales decreased high-single digits due to lower volume and price. PRO paint sales were up mid-single digits and DIY paint sales decreased low-double digits. A portion of this DIY decrease was driven by timing of sales across the first half of the year.

For the first half of the year overall, we saw total paint sales decrease mid-single digits with PRO paint sales up low-single digits and DIY paint sales down high-single digits. As we continue to experience overall softness in the DIY market, we now anticipate our full year DIY paint business to be down mid-single digits versus our previous expectation of down low-single digits. In our PRO paint business, we continue to expect sales to increase low-single digits.

Operating profit was $174 million, down slightly year-over-year. However, operating margin was up 80 basis points to 20.8%. Operating profit was impacted by lower volume and an unfavorable price/cost relationship, partially offset by cost savings initiatives and the timing of marketing spend.

Turning to slide 10. Our balance sheet remains strong with gross debt-to-EBITDA at 2 times at quarter end. We ended the quarter with $1.4 billion of liquidity, including cash and availability under our revolving credit facility. Working capital as a percent of sales decreased 50 basis points to 18.4% as we continue to stay disciplined on our working capital levels.

During the second quarter, we repurchased 2 million shares for $143 million and paid a dividend of $64 million to shareholders. As we previously guided, we continue to anticipate deploying approximately $600 million during the year towards share repurchases or acquisitions.

Now, let's turn to slide 11 and review our outlook for 2024. For total Masco, our top line for the first half of the year came in largely as expected. While we previously expected sales growth in the second half of the year, we are moderating our view and now anticipate sales to be roughly flat in the second half of the year and for our full year sales to remain within our previously guided range of plus or minus low-single digits.

With our strong first half execution and operating margin performance in our Plumbing segment, we now expect full year operating margin to be approximately 17% to 17.5%, increased from our previous guide of approximately

17%. And while we are seeing increased commodity and ocean freight cost across both of our segments, we expect to continue to deliver operating margin expansion in the second half of the year, with most of this to occur in the fourth quarter.

In our Plumbing segment, we are maintaining our top line expectation of full year 2024 sales to be plus or minus low-single digits versus the prior year. Based on strong execution in the first half of this year, we are increasing our expected full year operating margin to approximately 19%, up from our previous guide of approximately 18.5%.

In our Decorative Architectural segment, we are lowering our 2024 sales expectation to be down low-single digits year-over-year versus our previous guidance of plus or minus low-single digits. This change is primarily due to continued softness in the DIY paint market. Despite lower expected sales, we are we are maintaining our anticipated full year operating margin of approximately 18%. This would be up from our prior year margin of 17.8% and primarily driven by cost savings initiatives.

Finally, as Keith mentioned earlier, we are narrowing our 2024 EPS estimate to be in the range of $4.05 to $4.20 per share. This assumes a 220 million average diluted share count for the year and a 24.5% effective tax rate. Additional financial assumptions for 2024 can be found on slide 14 of our earnings deck.

With that, I would like to open up the call for questions. Operator?

QUESTION AND ANSWER SECTION

Operator: Thank you. [Operator Instructions] Your first question comes from the line of Matthew Bouley with Barclays. Please go ahead.

Matthew Bouley
Analyst, Barclays Capital, Inc.

Q

Good morning, everyone. Thank you for taking the questions. Maybe I'll start on Decorative. Thinking about the guidance for a low-single-digit decline for the year, and you're obviously tracking down, kind of, mid-single digits in the first half. Did I hear you correctly that you were saying paint would be down mid-single digits for the year? Just if you could clarify that relative to the total segment of down low-single digits, and I might have misheard you.

But in general, the question is around what's happening in DIY with this kind of deceleration here in Q2? And what are you assuming to expect some level of acceleration there in the second half to get to the full year guide? Thank you.

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

Good morning Matt, Keith here. Thanks for the question. I think when we think about the DIY, specifically DIY paint sub-segment, I think it's well-known that, that sub-segment tends to be more sensitive than other segments, sensitive to economic conditions, sensitive to affordability, sensitive to consumer confidence overall.

So, when you look – think about what's happened in the market, with regards to the price that's been put in, I think over the last couple of years, we're knocking out 40% price increases across our total company on average. So, there's a lot of pressure that's been put on that sensitive segment, rates being high, overall affordability in that whole consumer basket through gasoline to groceries to everything. So, it's well known that, that's a sense of segment and we expected it to be down.

I think when we look across regionally, it's pretty consistent. So, it's a little bit more pressured than we expected. I think we highlighted that in our remarks. Looking forward, why we have the guide where we have it is based on really three fundamental things. One is our comparables. When you look at the first half over the second half, our comparables soften a little bit, and that will be some tailwinds.

Secondly, we've talked about some of our SG&A spend being transferred from last year where it was in the second quarter to the third quarter this year. We're going to be using that to drive demand principally through advertising. We obviously have a lot of experience in that, and we know what to expect. And then, lastly, I would say that our guide contemplates – well, I'm not going to get into the specifics. Our guide contemplates what we're seeing in recent demand trends as we exit the quarter.

Richard Westenberg
Vice President, Chief Financial Officer and Treasurer, Masco Corp.
A

Yeah. And Matt, the only thing I would add to that, just to clarify the guide for the full year, what we indicated is that the DAP segment overall would be down low-single digits for the year. Within that, we indicated that Pro paint would be up low-single digits and DIY paint to be down mid-single digits. We didn't give an overall paint guidance, but you can assume that it's in line – from a total paint perspective, in line with the overall segment of down low-single digits.

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.
A

I think, Matt, when you think about how we've performed in this volatile time, not only in our Decorative Architectural segment, but across the company, and you see what we've been able to do with our margins as it relates to driving sticky and sustainable productivity enhancements across the P&L statement, and what we've been able to do with regards to price, which is an opportunity we have, given our strong brands and our innovation pipeline. This business has really handled this volatile market well, and we are in good shape.

And what's exciting is about what we have to look forward when this demand does return to more stabilized and more normal growth rates, we have this business dialed in to really contribute incremental earnings on that incremental volume. So, feel real good about both of our segments in terms of what we've been able to demonstrate in terms of performance.

Matthew Bouley
Analyst, Barclays Capital, Inc.
Q

Got it. Okay. Thank you for all that color and detail and for clarifying the guidance there. And then, so maybe shifting to Plumbing. Certainly, the top line result there in the second quarter, I mean, you did see, I guess, I would call it, acceleration in organic growth US and international. I mean, maybe across both US and international, what exactly is driving that? I mean, you gave some great color there on why DIY paint is having a specific issue, but perhaps here on the Plumbing side, you saw some better trends. So, just kind of any color on sort of the shape of demand and how you're envisioning demand continue to evolve in the Plumbing segment? Thank you.

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.
A

If you think about – I'll talk globally now, international versus domestic. We've started to see some demand challenges early last year in international – in domestic and then international lagged a couple of quarters. Last call, I talked about how I felt strongly that we've come to a stabilization point in North America. And whilst we were seeing signs of stabilization in Europe, I was a little reticent to call that a stable at that point, but it was moving in the right direction. I'll tell you that we continue to see more signs of stabilization in international, and I feel that we are in that period of stabilized demand internationally. So, that goes for our key markets in Central Europe, Germany, in particular, in China. So, it feels very much like it did a quarter or two ago in North America.

Internationally, the team at Hansgrohe continues to do a wonderful job, and we are clearly taking share there. And that's – while it's been consistent in talking about how it's difficult to nail down market size, specifically quarter-to-quarter. But when you look at our performance vis-à-vis our major competitors on the continent, we're doing a very good job and we're gaining share.

So, it's a combination of the market starting to come around, stabilization of demand, strong initiatives with regards to share gains and organic growth and a little bit of a slight bit of some pricing tailwinds where we've had some carryover pricing from last year. And that's some incremental spot pricing in parts of our assortment this year.

In North America, I can't say enough about the team in North America, continuing to do a very strong job of organic growth with influencer advocacy development that we've been focused on for about a decade, frankly, and that just continues to pay off, and we view that as a factory where we're producing advocates through our influencers where there is an assisted sale in showrooms, for example.

Our product assortment and our product launches in our spa business has been wonderful, and we've got a great assortment that continues to – and will continue to roll out. So, we've returned to growth in that – in our spa business. That's over and above the benefits of the acquisition of Sauna360. We think Sauna360 has some nice legs to it as we start to leverage our outstanding dealer network and get that brand more and that assortment more available here in North America. So, good hard work, and we anticipate that continuing.

And again, like my comments on your paint question – around your Decorative question, the margins are indicative of how well we're doing in operating our operating system. We have a pipeline of Kaizen and continuous improvement activities. That is across our P&L. We're working on variable cost productivity, with labor productivity, scrap rate reductions, overall equipment effectiveness improvements. We're working on variable cost productivity with regards to trying very hard and keeping a close eye and putting – taking shifts off-line and combining shift, maybe even working some overtime to enable us to take shift offline, so we can drive that sort of productivity. Those are sticky initiatives. So, looking forward, when this demand does return to normal, we're excited about the prospects of earnings and what it can do for shareholder value.

Matthew Bouley
Analyst, Barclays Capital, Inc.

Q

Excellent. Well, thanks, guys, and good luck.

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

Thank you.

Richard Westenberg
Vice President, Chief Financial Officer and Treasurer, Masco Corp.

A

[ph] Matt (00:26:59).

Operator: Your next question comes from the line of Stephen Kim with Evercore ISI. Please go ahead.

Stephen S. Kim
Analyst, Evercore ISI

Q

Yeah. Thanks very much, guys. Appreciate all the color. I had a couple of longer-term questions for you, though. I guess the first one relates to what adjustments you might make in the event that there's an abrupt change in tariff policy? And if – are there any lessons you learned from last time this happened that you would expect to apply in the future if needed?

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

Yeah. I think when you think about tariffs, when the original Trump tariffs, when they were enacted, we've been working very hard with our suppliers. I would tell you, Stephen, that in terms of moving to alternative sourcing solutions that would avoid tariffs, we've been able to reduce our exposure by approximately 30%. So, that's a big number. We've obviously been driving margin improvement initiatives that I've already talked about. I won't go into that as much. And we've demonstrated the ability to manage through it. And I think that's the best indicator of future performance is what we've been able to do in the past. And our margins are above pre-pandemic levels. So, it took some time, but we've been able to manage it.

So, should those tariffs come back into play, we have incentive systems that we've learned from how to appropriately guide the behaviors of our teams to address these issues in a quick fashion. We're starting from a better spot where we have 30% less of our buy tariff exposed. So, that's a big help. And we'll continue execute much of the same playbook that we did in the past. I think we'll do it more effectively. We'll do it more judiciously and faster based on our experience, but all of our key management teams have been through this, and we're keenly aware of it.

Stephen S. Kim
Analyst, Evercore ISI

Q

Yeah. That's very helpful. Thanks very much for that. And then, a broader question about your product portfolio. I was wondering whether you're actively seeking to broaden or narrow your product portfolio at this time. Anything specific that you might talk about. And as you look out over the next few years, how do you assess the key strengths that Masco brings to the table that makes you a better owner of certain assets.

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

So, in terms of our product portfolio and the question of broadening or narrowing, I think there's a couple of components to that. First, we begin with the consumer and we look at pain points that consumer is experiencing and try to find ways that we can resolve those pain points, and we continue to drive that. So, that's not so much with a lens on broad or narrow. It's more with a lens of can we meet an unmet need and do it efficiently and rapidly, get it to market, hopefully wrap some IP around it, so that can have some protection and then move on to the next innovation.

So, things as simple as how consumers clean their glasses in the sink and what we can develop to help them do that. How we can work with better technology to avoid germs on your hands and how we can activate various technologies to enable consumers to have their problems solved in the kitchen. We certainly are looking at environmental issues, and our ESG and you may have seen it in our sustainability report, where we're working hard on water conservation and how to utilize technology to give better shower experience at lower flow rates, for example. So, it's really about customer-backed innovation to meet an unmet need and to continue to leverage our brand, build our brand and give us that pricing power and that must-have position on the shelf. So, that's really the fundamental nature of where we're focusing our innovation.

In terms of narrowing, 80/20 is a fundamental component of our operating system, and we look at the long tail, and we understand the costs associated with that, and we know and we believe that there's no line item on the P&L that says complexity, but there is a cost to complexity. And so, we're keenly aware of cutting that long tail to be as productive as we can and save those costs to put back into a combination of more growth and higher margins. So, it really is a two-edged sword of unmet customer need and complexity reduction.

In terms of the key strength of Masco, really, there's brand service and innovation are the strengths that we bring to the market. And coupled with that is strong customer and channel knowledge that we leverage across our product assortment. So, when you look at our portfolio, you see that we've – as we've talked before, Steve, that we've really pruned our portfolio down to where we now have very similar businesses that performed very similar in terms of margin profile or capital requirements, low ticket and we're able to leverage our channel expertise and our expertise as it relates to supply chain management across these businesses to make what we believe is our portfolio is more valuable, because they're part of our portfolio, and that's our view.

Stephen S. Kim
Analyst, Evercore ISI

Q

Okay. I appreciate that very much, guys. Best of luck with the rest of the year.

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

Thanks, Steve.

Operator: Your next question comes from the line of John Lovallo with UBS. Please go ahead.

John Lovallo
Analyst, UBS Securities LLC

Q

Good morning, guys. Thanks for taking my questions as well. The first one, Keith, just talking about some of the cost savings initiatives and efficiencies that have been in place. I'm curious how you guys think about the sensitivity of your EPS guide to the top line? And what I mean is that if sales were to come in at the lower end of the range, do you think you could still sort of achieve the midpoint, maybe even the higher end of the EPS range just on the cost saves and execution?

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

Yes, I do. And the reason, John, is because of the nature of the improvements that we've done, we're not hoping on things to happen in the future to enable us to hit our margin targets. We are confident in being able to hit our margin targets because of the pipeline we have for execution going forward, and because of what we've done and completed. And those are things that are sticky, that the teams have done an excellent job of executing against and we remain confident in.

We do have a demonstrated ability over time to price and to get a fair price, and we've earned that with our expense and our spend, brand, our innovation pipeline, how we do in terms of service, our advocacy with the channels that we've driven, to help us get that kind of must-have position on the shelf. So, yeah, we're confident, we will hit our margin targets.

John Lovallo
Analyst, UBS Securities LLC

Q

Okay.

Richard Westenberg
Vice President, Chief Financial Officer and Treasurer, Masco Corp.

A

Yeah. And John, the only thing I would add is, as you obviously saw from our comments this morning, we've tempered our expectations for the second half of the year, and that's factored into our guide. And even in spite of – despite the lower or tempered expectations for sales, we've narrowed our guide keeping that midpoint. And we're confident we'll end within that EPS guide range.

John Lovallo
Analyst, UBS Securities LLC

Q

Okay. That's helpful. And then, can you guys comment on the June exit rates for both businesses? It seems like Plumbing may have actually been positive as things exited. Any kind of help you can give us on what July trends are? And then, within that, why is PRO paint hanging in there so strongly, given kind of the softness in some of the overall economic metrics and things of that nature?

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

Yeah, John, I'll comment on exit rates coming out of the quarter. And it's – there's – when you look at quarter versus prior year quarter and what happens on the edge of one quarter in the following quarter, one year and then the previous quarter to next year, it makes that in itself can throw some complexity and some murkiness into how we look at the business.

When you start parsing out to how we exit quarters and where the months are and what happens inter-quarter, that gets even worse. So, we don't do that. But I will tell you that our exit rates and our run rates at the end of the quarter and through July are contemplated in our guide. So those are factored in. Can you help me out with that second question ahead, John, PRO paint?

John Lovallo
Analyst, UBS Securities LLC

Q

Yes. What is keeping PRO so strong in your opinion?

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

I think it's a couple things. One is the nature of the consumer who uses PRO versus the DIYer and how sensitive they are. And we're seeing that, call it, a mix dynamic. In this case, it's a, call it, a mix of who does your installation, you hire a PRO. But we're also seeing that in terms of the high end of our assortment in Plumbing and then some of the high-end assortment in Deco, where it's just less sensitive. So, people who tend to use a PRO are less sensitive to some of the macroeconomic uncertainties and consumer confidence issues that are around. They're a more robust consumer, because they're a little more affluent. So, I think that's a piece of it.

The other piece is our performance and our share gain, which we continue to drive and to hold. So, I think that really sheds a little bit light from my perspective on why PRO is performing a little bit better than DIY, why the upper end of our assortment across the whole business is hanging in there a little bit better than the lower end of our assortment. And it really has to do with the subsegment of the consumer base and how sensitive they are.

John Lovallo
Analyst, UBS Securities LLC

Q

Okay. Thank you, guys.

Operator: Your next question comes from the line of Adam Baumgarten with Zelman & Associates. Please go ahead.

Adam Baumgarten
Analyst, Zelman & Associates

Q

Hey. Good morning, everyone. If we think about DIY, where do volumes currently sit compared to pre-COVID levels in paint?

Richard Westenberg
Vice President, Chief Financial Officer and Treasurer, Masco Corp.

A

So, Adam, it's Rick. So, DIY volumes are below where we were pre-pandemic. PRO volumes are above where we were pre-pandemic. And so, overall, we're relatively consistent in terms of pre-pandemic. Obviously, the mix has changed. And as Keith – obviously, we articulated DIY is more challenged given the factors that Keith articulated, but PRO is performing. And as you may recall, we had incredible growth in PRO really from 2020 to 2023, really 60% stacked comp in terms of growth and that's really more or less offset the DIY headwind that we're facing. That said, we've been able to really hold on to our margins in that environment, and we're really positioned well, both in PRO and DIY from when the market turns to growth again.

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

Adam, I might add on to that and expand a little bit on your question, which was specifically on PRO paint, pre-pandemic to now and back up and take a broader look at our entire company and our whole assortment as it relates to our performance pre-pandemic to where we are today.

And I do so because I think it tells a very interesting story for our investors. When you look at pre-pandemic levels of volume and you extend that out to traditional growth rate of, say, 2.5%, you get to where we are today. What you'll see and a little bit of timing differences. But broadly speaking, when the pandemic hit, we had very substantial bump in our demand and then that demand went below the historical run rate extended from pre-pandemic levels and we went through that pull forward, if you will.

And when you look at where we are now in terms of volume and you inflation adjust that COVID bump because there was significant pricing in there, so you really look at where the volume is, what you see is a deferral of demand, we believe, and that the size of that deferral, that area under the curve is roughly the same as the – as what we saw post pandemic, inflation adjusted. So, our view is that we really are seeing a deferral of spend in the DIY space. And that's exciting for us, because as we've talked quite a bit already today, our business is tuned in, and that's – the measure of that is our margins.

And we have a state-of-the-art new paint plant coming up in Ohio, and that ramp-up is going fabulously, the team is doing a great job. We have a significant, very large Plumbing manufacturing plant in Serbia, that's coming online. And again, same story. All things are going well, and that plant is coming up nicely. So, as this demand starts to return to normalized levels, we've got the business tuned with regards to our cost control. We're watching our SG&A spend closely on the growth incentive – or growth investments. And our capacity is in great shape to be able to support it, including some surge capacity for selling seasons on our paint side. So, this business is ready to do some exciting stuff when this market turns.

Adam Baumgarten
Analyst, Zelman & Associates

Q

Okay. Got it. Good to hear. And then, just in Plumbing, a couple of questions. Just if you could walk through kind of how North American growth trended across retail and wholesale? And then, you mentioned negative mix in the segment. Maybe what drove that?

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

A couple of components. We are seeing some trade down in the assortment while the upper entity assortment is holding on very well, as I talked a little bit earlier. There is a little bit of trade down from mid to the lower part of our assortment, understanding we don't play in the very low piece of the assortment. So, there's a bit of trade down. And then, there's also a bit of geographic mix where earlier on, we're seeing it more stable now for sure, but China was challenged for a couple of quarters. In China, for us, with our hottest growing AXOR brand tends to be a higher end consumer. So, as geographically, as China goes down, that's a natural mix. Now, having said that, we – Rick, I don't think we're really calling for much of an impact in mix for the year. No.

Adam Baumgarten
Analyst, Zelman & Associates

Q

Thank you.

Richard Westenberg
Vice President, Chief Financial Officer and Treasurer, Masco Corp.

A

Yeah. Adam, to your question about channel performance, there's a bit of noise quarter-to-quarter from a comp comparable perspective. So, I'd like to think about it really from a first half perspective. And really, we saw solid kind of low-single-digit growth in kind of the wholesale trade and retail held up actually reasonably well. And we're expecting that trend to continue in the second half of the year as we've guided for the segment overall, plus or minus low-single digits. So, we're seeing stability. And also, on top of that, some pricing that led to some favorable price/cost relationship as well that's adding to our margin expansion for the year.

Adam Baumgarten
Analyst, Zelman & Associates

Q

Hey. Got it. Best of luck.

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

Thanks, Adam.

Operator: Your next question comes from the line of Michael Rehaut with JPMorgan. Please go ahead.

Q

Hi, everyone. Thanks for taking my question. This is [ph] Andrew (00:42:22) on for Mike. I just wanted to ask maybe high level thinking about your repair and remodel outlook with some potential rate cuts here and some pressure on the existing home sales. Just curious if you're leaning more towards the upside or downside on that outlook? Thanks.

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

Not really leaning it away or kind of right in the middle. We're calling R&R to be flat to down low single digits, and I think that's the right place to be.

Q

Got it. And then, in terms of commodity volatility, just curious on how you're thinking about input costs across segments and pricing to offset that?

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

Go ahead.

Richard Westenberg
Vice President, Chief Financial Officer and Treasurer, Masco Corp.

A

Sure, [ph] Andrew (00:43:10). It's Rick. So, from a commodity perspective, I'll take a step back overall. Really, in Q2, we didn't see a significant driver one way or the other. In the first half of the year, we saw commodities be a slight tailwind to our performance. And in the Plumbing segment, we have positive price/cost relationship.

As we think about where we sit here today, as I think we've all observed, we've seen a bit of an uptick with regards to the metal prices of copper and zinc. It has trailed off a bit, but still elevated, as well as some of the pain inputs. So, TiO2 and resin, there's some pressure in that. So, we see that as – as I mentioned in my opening comments, we see that as a bit of a headwind in the second half of the year. Now, granted it takes time for the commodity costs and ocean freight costs for that matter to work its way through our inventory and hit our P&L. But given the inflation that we saw really during the quarter, we do expect to have that be a bit of a headwind in the second half of the year, really later in the year. Despite that, we actually are, as you know, expecting margin expansion in the second half of the year, really in both of our segments. And so, we're able to overcome those headwinds. We're monitoring that very closely, and we're taking action accordingly. But we do expect to have margin expansion in the second half of the year and margin expansion overall. And thus, we've raised our operating profit margin expectations for the year.

Q

Really appreciate that additional color. Thanks, so much. Good luck.

Operator: Your next question comes from the line of Anthony Pettinari with Citigroup. Please go ahead.

Anthony James Pettinari
Analyst, Citigroup Global Markets, Inc.

Q

Good morning. For DIY paint year-to-date, do you think your volume performance has been sort of in line with kind of the underlying DIY market? Or have your volumes maybe tracked a little bit better or a little bit worse than the industry? And if there's any sort of variance there, what do you think is driving it?

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

Anthony, it's -- and I've talked about this really across our entire company. But particularly when you talk about getting into subsegments of DIY that go through multiple channels and it's very difficult to accurately pin down market size, particularly from one quarter to the next. So, that's a major caveat here. But when we look at where we performed in the first half of the year, because there was a little bit of some system fill volume that last year was in the very beginning of the second quarter that this year was in the last – end of the first quarter. So, when you look at it for the first half, and we look at how we are performing versus what we can tease out from what we hear from our competition, and that's not easy as well. Sometimes you have to really listen hard to understand what is DIY versus what is in a particular segment, how much of DIY is in another segment, et cetera.

But we think we're right there. We think we're holding share and that's attributable to a couple of things. Obviously, we have an outstanding partner in the Home Depot who does a phenomenal job of generating foot traffic and merchandising and with our partnership with some 40 years, it's very productive as we're both focused on the same thing, which is serving the customer. So that's a big piece.

And then, Behr brand. When you look at the Behr brand, I can make a very strong argument that we are the best DIY brand out there. And that's based on collaboration from outside sources, whether you look at quality or service or brand in terms of both awareness and equity. So, I feel extremely good about our business, knowing full well that the DIY channel is a bit challenged now. And again, as I've said before, when this starts to turn around, we are ready with surge capacity. We're ready with a tuned in cost structure as demonstrated by our margins, and the team is fired up. So, I think we are holding our own.

And certainly, when you look at the PRO side of the business, not only gained some significant share over the years, but demonstrated the ability to hold it. And with – frankly, our lower piece of the total market, we have a lot of white space and a nice value proposition that we're going to continue invest in.

Anthony James Pettinari
Analyst, Citigroup Global Markets, Inc.

Q

Okay. That's very helpful. And then, just we've seen existing home sales fall below 4 million, really historically low levels. And I'm just wondering how that is impacting different parts of your business. If you can just kind of remind us maybe which parts of Masco are most impacted or maybe at least impacted by the slowdown in existing home sales in the US.

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

More existing home sales is better for us than last particularly when you talk about paint and people paint their homes before they sell, the new owner paints it to their taste. But when you really peel back the numbers, it's not much of an impact, really. I mean, if you're talking about 4 million to 5 million existing home sales on a 130 million base. And when you have an existing home turnover, that might – I think the number is somewhere around 25%, 30% increase in DIY spend for that period during the transition. So, you take 4 million out of 130 million and you get a 20% bump on those, it's very, very – really very low impact. We're a small ticket repair and remodel portfolio, purposefully tuned into that to give stability and resilience through cycles and to deliver double-digit EPS through cycles for the investors.

And the key correlation there is consumer confidence, existing home equity. And we – that's why, we feel so good about it. So yes, obviously, more is better in terms of existing home turnover, but it's not that material for a business when you really look at the numbers.

Anthony James Pettinari
Analyst, Citigroup Global Markets, Inc.

Q

Okay. That's very helpful. I'll turn it over.

Operator: Your next question comes from the line of Mike Dahl with RBC. Please go ahead.

Q

This is [ph] Chris (00:49:36) on for Mike. Just going back to the DIY paint comments. I think earlier you said – you made a comment around a more sensitive consumer in DIY. I mean, how would you characterize the dynamics of DIY today relative to kind of what you saw last quarter? And then, within the down, low double-digit sales decline in 2Q, any way you could break out what price versus volume looked and your expectations on both those drivers in the back half, that would be helpful? Thanks.

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

I don't think there's really any difference in the DIY perspective this quarter from last quarter. I don't have any technical numbers on a quarter-by-quarter basis to say that. But just talking and being in the channel and getting exposed to our business, I really don't see a difference. As far as the low double-digit down in DIY, you really have to look at the half, as I said, because there were some volumes that straddle one quarter versus the other quarter when you look year-over-year.

Richard Westenberg
Vice President, Chief Financial Officer and Treasurer, Masco Corp.

A

Yeah. [ph] Chris (00:50:35), I mean, just to add more [indiscernible] (00:50:37). That's why, we look at it really – we think it's appropriate to look at it from a first half perspective. And as we mentioned, DIY was down high single-digits in the first half of the year, and that was – there wasn't really any trend per se within the half to focus on.

I think to your other question, as it pertains to volume and price, we haven't broken down specifics, but they were both headwinds. Price was a low single-digit down and then volume is remainder. And as I know, we've articulated in the in the past, we've got a relationship with the Home Depot in terms of an agreement in terms of price, commodity cost neutrality.

And so, what we saw is we saw commodity cost decrease in the second half of last year. And as a consequence, as we mentioned previously, we provided some price downs as part of that. And so, that's what you're seeing manifesting itself this year. It's really carryover price implication. And we'll see that kind of carry through the second half of the year. But as articulated, we do see improvement in DIY paint as we enter the second half of the year, some of it is a comp dynamic, some of it's really actions taken by the team. And we do expect that ultimately for the year, DIY would be down mid-single digits based off of those actions.

Q

Understood. That's helpful. And then, just shifting over to Plumbing. How do the channel inventories look today? Is there any kind of notable restock or destock dynamics that we should be aware of?

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

No. I mean, there's always seasonality adjustments to get ready for selling seasons, but nothing really out of the ordinary.

Q

I appreciate the color.

Operator: Your next question comes from the line of Sam Reid with Wells Fargo. Please go ahead.

Sam Reid
Analyst, Wells Fargo Securities LLC

Q

Thanks, everyone. I wanted to talk about the Dec Arc segment, but maybe focus on the lighting business for a moment here. I think you made some moves to stabilize this last quarter. Looks like growth might have improved sequentially in lighting, if my math is correct. Just remind us what you've been doing here, because you've done streamlining the subsegment. And what are the opportunities to kind of further stabilize top line here?

Richard Westenberg
Vice President, Chief Financial Officer and Treasurer, Masco Corp.

A

Yeah, Sam, I appreciate the question and good memory. So with regards to the lighting business, we – the team has taken some really proactive actions with regards to opportunistic pricing, streamlining lines of business, exiting lines of business that had less profitable dynamics to them and of course, cutting cost and really has positioned the business for success going forward. We don't provide, as you know, breakdowns of financials within our segment. And what I would say is the top line performance has improved sequentially, and we're expecting that the lighting and hardware business, which are the complements to paint in the DAP segment, to be really going forward that performance top line to be in line with the R&R industry expectations, which as Keith articulated earlier, it would be flat to down low single digits. But we're definitely seeing a positive trajectory relative to where we were, let's say, a few months ago.

Sam Reid
Analyst, Wells Fargo Securities LLC
Q

That's helpful. And then, I wanted to switch gears and dig a little deeper on Plumbing really quickly, but maybe in the context of pricing. Are there – were there any noticeable differences in pricing between channels, I'm thinking wholesale versus retail here? And then, thinking in terms of kind of what's embedded in your outlook for 2H kind of any divergence in pricing we should be thinking of from a channel perspective, again, kind of retail versus wholesale? Thanks.

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.
A

Yeah, Sam. I would say from a pricing perspective, we can speak overall, which was it was for Plumbing for the segment, it was a positive 2% contributor in the quarter. From a channel perspective, we don't get into that specifically. I would say that from a trade perspective, it's pretty robust. But I would say that we're – the team is really focused on taking price in reflection of our strong brands in our portfolio – in our product portfolio and really capturing that value. But we generally work hand in hand with our customers to make sure that we've got really profitable growth across the ecosystem. But I would say I would stick to in terms of our expectations, our results and our guidance really at a segment level, and that's positive low single-digit pricing this quarter and for the year.

Sam Reid
Analyst, Wells Fargo Securities LLC
Q

Thanks so much. I'll pass it on.

Operator: Your next question comes from the line of Susan Maklari with Goldman Sachs. Please go ahead.

Susan Maklari
Analyst, Goldman Sachs & Co. LLC
Q

Thank you. Good morning, everyone. My first – good morning. My first question is, you mentioned that you did see some benefit on the cost savings and some of those broader initiatives that you've been working on in the quarter across both of the segments. Can you just talk a bit more about what some of those were, how they've come together? And I guess, as you think further out, the ability to continue to realize those benefits as you try and close that margin gap with where we are today relative to the longer-term guide?

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.
A

So, to give you a little bit of flavor for it, because our pipelines are very large, and we measure the Masco operating system measures and drives our performance this way by taking down a gap that we want to attack and putting it into a module of continuous improvement that we can execute on, we call a Kaizen event.

And we measure those in terms of where they are in the pipeline in the five-step process and how we drive them through. We look at size and we look at flow-through and then we have finance, validate what the actual benefit is. So we make sure that we're putting in – into the P&L. So, they're pretty small and discrete items. And the benefit of that is that the ability to manage these improvement initiatives through the system is what our leadership profile is really about.

So, it's not only helping to develop our business in terms of margin and performance, but it's also developing our leaders. So, my point is they're pretty small modules. So, things like identifying a capacity constraint in a particular area of our business where demand has taken off more than expected and being able to drive improvement in that capacity, so that we are more efficient. And that the rest of the factory isn't waiting on that output. That's a big output from a small event that we've done over time, multiple events. So, that's on equipment productivity.

On people productivity, it's about balancing shifts and taking shifts instead of running a half shift on second shift, which takes maintenance personnel and supervisory personnel. We jam that into one shift, and then we're able to get more productive on the semi-variable overhead and then do a series of Kaizen events on that shift that's working overtime to sustain to give us off over time, that sort of thing.

It's – on the top line, it's coming in with growth initiatives and how we can execute better through sales force execution, whether it's better segmentation or better standardization of how we make our sales call, so that we are more effectively highlighting the benefits versus the competition. And these are all things that we can train to in our leadership and in our salaried folks, so that, as I said, it's developing our leaders as well. So, it's a series of small steps that we click through and then work very hard to avoid back stepping.

Susan Maklari
Analyst, Goldman Sachs & Co. LLC

Q

Okay. That's great color. And then, turning to capital allocation, you still are on track for that $600 million of repurchases or bolt-on M&A. Any comment on M&A, how that pipeline is looking? Anything of note there?

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

Not a whole lot of change from the last quarter. I would say we are feeling that there's – it's still a little quiet out there with where rates are and where valuations are and where people who are ready to sell – aren't so ready to sell and a little bit of a deflated – what we're seeing to be little bit of a lower valuation sort of period. But there's plenty of work that we're out there for us, and we're evaluating it.

I'll tell you, Susan, that our capital allocation strategy has not changed. We're focused on paint and Plumbing and looking for businesses that we can learn from and that we can leverage. I think Sauna360 is a great example of what we're looking for. It was a smallish, call it, $100 million business in that range. But one that when we are able to look at that technology and what they offer, we can bring a significant amount of value creation to that business through our extensive dealer network in the United States. That's the sort of thing that we continue to work on. And I would say, deal flow is about the same as it was before.

Susan Maklari
Analyst, Goldman Sachs & Co. LLC

Q

Okay. That's great color. Thank you. Good luck with everything.

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

A

Thank you.

Richard Westenberg
Vice President, Chief Financial Officer and Treasurer, Masco Corp.

A

Thanks, Sue.

Operator: Your next question comes from the line of Keith Hughes with Truist. Please go ahead.

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

Q

Thank you. Earlier in the call, you would discuss some inflation – input inflation coming. In terms of offsetting that, do you think we'll be using price increases and you can talk about that paint versus the Plumbing segment?

Richard Westenberg
Vice President, Chief Financial Officer and Treasurer, Masco Corp.

A

Yeah. Good morning, Keith. Sure. So, as you alluded to, and I mentioned in my opening comments and during an earlier Q&A, we do see some commodity inflation and ocean freight – elevated ocean freight here that it's going to be serving as a bit of a headwind as we enter the second half of the year. Specific to your question, we do see pricing in the Plumbing segment as an offset to that. Really, we're continuing to take low single-digit price increases with regards to our Plumbing segment. We'll continue to lever that. But really, that's a Plumbing dynamic. As it pertains to the coatings, it's really going to be a balance between where we end up relative to commodity or input costs and our net price with regards to our retail partner in that regard. So, really no comment there.

I would say, though, in addition to price, as Keith has alluded to a couple of times, the team has done tremendous work with [ph] Behr to (01:01:11) driving operational efficiencies and cost down. So, with regards to offsetting that commodity headwind, it's certainly, price is part of the equation, but it's not exclusively priced. It's also operational efficiency, cost reduction and running the business tighter. And we're seeing that here in the first half, and we'll continue to drive that in the second half of the year to deliver the margins overall that we've guided to.

Keith J. Allman
President, Chief Executive Officer & Director, Masco Corp.

Q

Okay. Thank you.

Robin L. Zondervan
Vice President, Chief Accounting Officer and Investor Relations/FP&A, Masco Corp.

We'd like to thank all of you for joining us on the call this morning and for your interest in Masco. That concludes today's call. Have a wonderful day.