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OVERVIEW:

Company Summary

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PRESENTATION

Operator

Good morning, and welcome to the Acuity Brands Fiscal 2024 third quarter earnings call. (Operator Instructions) Please be advised that today's conference is being recorded. I would now like to hand the conference over to Charlotte McLaughlin, Vice President of Investor Relations. Charlotte, please go ahead.

Charlotte McLaughlin - Acuity Brands Inc - Vice President of Investor Relations

Thank you. Good morning and welcome to the Acuity Brands Fiscal 2024 third quarter earnings call. On the call with me this morning are Neil Ashe, our Chairman, President, and Chief Executive Office; and Karen Holcolm, our Senior Vice President and Chief Financial Officer. Today's call will include updates on our strategic progress and our fiscal 2024 third quarter performance.

There will be an opportunity for Q&A at the end of this call. As a reminder, some of our comments today may be forward looking statements. We intend these forward-looking statements to be covered by the Safe Harbor provisions of the Private Securities Litigation Reform Act of 1995. As detailed on slide 2 of the accompanying presentation.

Reconciliations of certain non-GAAP financial metrics with their corresponding GAAP measures are available in our 2024 second quarter earnings release and supplemental presentation, both of which are available on our Investor Relations website at www.investors.acuitybrands.com. Thank you for your interest in Acuity Brands. I will now turn the call over to Neil Ashe .

Neil Ashe - Acuity Brands Inc - Chairman of the Board, President, Chief Executive Officer

Thank you, Charlotte, and thank you all for joining us this morning. In our fiscal 2024 third quarter, we delivered solid results. We increased our adjusted operating profit, adjusted operating profit margin and adjusted diluted earnings per share.

We generate strong free cash flow and we allocated capital effectively to drive value. In our lighting and lighting controls business, we continued to expand profitability while we focus on returning the business to growth.

In our Intelligent Spaces business, the growth rate and overall performance remains impressive. In ABL, we increased our adjusted operating profit \$2 million to \$162 million and increased our adjusted operating profit margin 100 basis points to 18% on \$42 million less sales. These results are

being driven by our ongoing efforts to increase product vitality, elevate service levels, use technology to improve and differentiate our products and how we operate the business and to drive productivity.

We define product vitality as a combination of new product introductions and improvements to our existing portfolio with the intention of making products that are more valuable for our customers and more profitable for us. A great example of this is the last (inaudible), which we recently introduced to the market. This luminaire as a modern and sustainable alternative to traditional LED panels and can be in all indoor applications, including commercial office and [Taser] 12 schools.

Frame offers our customers value as a result of three things. The first is flexibility of design. The frame comes in three different size options with switchable technology to offer different [lumen output] and color temperatures.

The second is it's lightweight design and patented snap connections that allow for quick assembly and ease of installation. And the third is that it costs less to package and ship as a result of it's minimal, sustainable packaging.

I'd now like to spend a few minutes talking about our differentiated product portfolios made to order, design select and contractor select and how they are creating the most effective way for our end users and contractors to get what they need, when they need it for their specific projects. The majority of our products are made to order, which uses our entire portfolio to create limitless design options for our customers. From concept to creation, we meet their requirements.

I'd like to share a few examples with you. We've been working on the restoration of the Michigan central station in Detroit, where with the original lighting blueprints from 1912 and recreated them as current generation LED fixtures. When combined with our controls, these fixtures, deliver energy savings and create distinct event lighting to deliver a completely unique solution. We are also able to adapt our existing lighting and lighting controls portfolio.

For example, this quarter, we met the retrofit requirements of a large retail customer by using the base design of several key fixtures and combining them with our controls to create a unique tailored solutions.

And finally, we have specialty brand known for innovation like Alight, Luminous and Eureka, which meet the needs of lighting, specifiers and different spaces ranging from offices to health care to schools.

Next, design select takes to eliminate this design options for made to order and curate them into an offering that delivers a highly productive approach to project design with either selection and service predictability. Whether our customer needs their products in three weeks or three months, we were able to satisfy their time lines. We deliver highly configurable product options for superior solutions by incorporating a broad portfolio of our trusted brands and offering end light embedded controls.

And the final part of our differentiated portfolio is contractor select. About 300 high volume products that are used in common everyday lighting applications, designed to be stocked and result. We have been able to create a portfolio that offers quality products that our customers one at competitive prices, while at the same time allow, we are distributor partners to achieve higher returns. We also continue to make investments for future growth. Prioritizing new verticals, where we have not historically competed or where we are underpenetrated.

We have recently entered the refueling vertical, which includes service stations, convenience stores and quick service restaurants. We are reimagining the cuts -- reimagining the customer experience using solutions specifically developed for these applications.

In addition to our other existing products sales from our lighting and lighting control portfolio. This is the vertical where we have not broadly completed. And earlier this week, we have announced and we have signed one of the leading independent sales agents positioning us well to compete in this established and growing market. This builds upon our discussion last quarter around entering the horticulture market.

This is another example of a vertical where we had not historically competed and where we have long-term opportunities for growth. We continue to be recognized by the industry. This quarter, we were awarded three Red Dot Design Awards for product design. One of the most sought after distinctions for design and quality.

We won for in-line by Luminous, which we profiled in our first quarter earnings call. [Fatal] by Eurika and Mochi by Cyclone. Fatal is a high-performance rain fixture with an elevated design that produces an evenly distributed glow and is available with multiple size and mounting options for use in commercial spaces and other indoor environments.

2024, marks the tenth consecutive year that our Eurika brand has won a Red Dot Design Award and Fatal brings us total product wins in this category to '20. Mochi is a contemporary zone street lights that offers precision elimination for use in infrastructure projects where safety is a priority, including city, residential street, and commercial buildings. It's innovative design offers multiple configurations in addition to a patented latch that allows for easy maintenance access without compromising security. This is the first red dot when for our cycle purity.

In addition, we were awarded 21 Bright Star Awards from LEDs magazine, which acknowledges innovation and lighting, components and controls. For products across 14 of our brands, including [active lux] [Hydrils] and [NN Life].

Now moving on to our Intelligent Spaces group. Our mission and our intelligent spaces business is to make spaces smarter, safer and greener through our strategy of connecting the edge to the cloud.

Distech has the best edge control devices in the market while Atrius will be the best in cloud applications. In spaces, we are focused on where we compete and what we can control to expand our addressable market. As part of our geographic expansion this quarter, we continued to add systems integrator capacity in the UK, Australia and Asia.

We partner with the best SIs in specific geographies to sell our full suite of Distech and Atrius products. In May, we hosted our key SI partners and end users at our European Connect Conference in Marseille. It was a great success, and we look forward to hosting our North American Connect Conference in Nashville later this year. At Connect, the Distech resets move sensor that we discussed in the first quarter continued to generate positive reviews.

As a reminder, this is an advanced seven in one ceiling mounts at sensor that is able to detect occupancy and provide feedback on occupancy and requirements and build spaces. We also showcased our refrigeration offering, which included the upgraded Distech key to term smart access, a personalized secure portal that provides real-time refrigeration system data that can troubleshoot system issues, prevent unnecessary [bot] site visits and save our customers money. The device talks to us all Distech term sensors and controls and allows on-site and remote monitoring for one or multiple site locations.

And this quarter, our spaces products received recognition from several industry leaders. Our Distech resets move, one best AI tech innovation for intelligent buildings at [ICON] 2024 last week, having also won an Excellence Award in 2024 electrical review and data center review earlier in the quarter.

Our Distech Controls Eclipse Apex controller, won a Product of the Year Award at the 2024 consulting specifying engineer awards. And Atrius won best ESG in climate reporting software from ESG investing magazine for the second consecutive year and won top product of 2024 by ENE leader. Now turning to our outlook, in our lighting business, our order rate continued to grow year-over-year in the third quarter. We built backlog as our orders exceeded our shipments. This backlog will be served in the coming quarters.

As we enter the fourth quarter, the order rate trend is likely to continue, and we will remain focused on returning the business to growth while expanding margins and generating strong free cash flow.

Our Spaces business continues to grow impressively and is becoming a more important part of our company. Our performance is and continues to be strong, and we will continue to allocate capital to expand our addressable market.

Now I'll turn the call over to Karen, who will give you an update on our third-quarter performance.

Karen Holcom - *Acuity Brands Inc - Chief Financial Officer, Senior Vice President*

Thank you, Neil, and good morning to everyone on the call. We continue to deliver solid performance in our third quarter with both our Lighting and Spaces businesses delivering margin improvement. We increased our adjusted diluted earnings per share, and we generated strong year to date operating cash flow.

We allocated capital effectively and continue to make progress on our strategic priorities. For total, AYI we generated net sales in the third quarter of \$968 million, which was \$32 million or 3% below the prior year as a result of the lower net sales in our lighting and lighting controls business.

Our Spaces business continued to experience strong growth of 15% in the quarter. We continue to deliver year-over-year margin improvement. During the third quarter, our adjusted operating profit was up \$4 million from last year on a \$32 million decline in sales, and we expanded our adjusted operating profit margin to 17.3%, an increase of 100 basis points from the prior year.

This increase was driven largely by the significant year-over-year improvement in our gross profit margin, and we continue to exit our strategy and drive margin through product vitality, the management of price and cost and productivity improvements. During the quarter, our adjusted diluted earnings per share of \$4.15 increased \$0.4 or 11% over the prior year, due to higher net income and lower shares outstanding.

In ABL, net sales were \$899 million, a decrease of 5%. However, as Neil said earlier in this call, our order rates are higher year-over-year. While the independent sales network was down as a result of the challenging comparable last year. This quarter was a good quarter for corporate account, which benefited from a large retail relight project.

Adjusted operating profit increased to \$162 million on lower net sales, while we delivered improved adjusted operating profit margin of 18% and 100 basis points improvement over the prior year.

Net sales and Intelligent Spaces for the third quarter were \$76 million, an increase of 15% of this debt continued to grow. The integration is key to term is now complete and keeping them products are now product line under the Distech controls product portfolio. Adjusted operating profit and intelligence basis was \$17 million, with the adjusted operating profit margin at 22.9%, a 340 basis points improvement over the prior year.

Now turning to our cash flow performance. We generated \$445 million of cash flow from operating activities year to date, and we are earning attractive returns on the cash that we have on our balance sheet.

We continue to allocate capital consistent with our priorities. Year to date, we invested \$41 million in capital expenditures. We acquired the assets of Arise Horticulture lighting, we increased our dividend per share 15% and allocated approximately \$89 million to repurchase over 454,000 shares. Since the beginning of the fourth quarter of fiscal 2020, we have repurchased approximately 9.5 million shares at an average price of about \$145 per share, which was funded by organic cash flow. This amounts to about 24% of the then outstanding shares.

We continue to demonstrate solid performance. We delivered improved margins and increased adjusted diluted earnings per share. We generated strong cash flow from operations, and we continue to allocate capital effectively. Thank you for joining us today. I will now pass you over to the operator to take your questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Christopher Glynn, Oppenheimer.

Christopher Glynn Glynn - *Oppenheimer & Co. Inc. - Analyst*

Thanks. Good morning. Looking at the continuing gross margin performance in all the execution there, curious if the service model streamlining initiatives, particularly the deployment of design select is pacing a faster than expectations perhaps?

Neil Ashe - *Acuity Brands Inc - Chairman of the Board, President, Chief Executive Officer*

Hey, good morning, Chris. Thanks for the question. So we're pleased with our performance on margin expansion. As you know, this has been a multiyear process, and it's been focused really on the strategy of product vitality, increasing service levels, using our technology to different and how we operate the business and then driving productivity.

So this is a point on that path. I'd highlight really around product vitality and our ability, as we said in the prepared remarks to both deliver more value to the -- to our end users as well as make more -- make product profitable for us.

So obviously, that's a number of things design select is among those things. It's actually pacing where we expected. So it is not the primary driver of the improvement here, which highlights the trend that we're on and the length of the path we still have the travel there.

So we're pleased. I'd also highlights that you'll remember we acquired the Optotronic business from Osram. So we control more of the technology that is in our luminaire. That gives us significant flexibility, both in our design and our operation. So we're pleased with the continued and performance and it is attributable to multiple different things working in harmony.

Christopher Glynn Glynn - *Oppenheimer & Co. Inc. - Analyst*

Thanks. Appreciate all that color. And then the positive book to bill notable, an interesting caveat the revenue being a little short of estimates out there, and I think it's from third straight quarter of positive year-over-year orders. I'm curious if the patterns weekly, monthly are still pretty consistent or perhaps they're getting a little more streaky in the front month or two?

Neil Ashe - *Acuity Brands Inc - Chairman of the Board, President, Chief Executive Officer*

Yeah. So this quarter, as we said, our orders exceeded our shipments. The order rate has been relatively consistent throughout the year. So as Karen mentioned in her remarks, our production target -- we did not meet our production targets in the quarter, which is our -- we built backlog. So why our orders exceeded our shipment. So we're working on that. We'll sort that out obviously going forward and we will satisfy that backlog.

The big picture, we are cautiously optimistic. I would say about the future, the power of the diversity of our portfolio is really demonstrating instead of both in this quarter and as we go forward.

So I'd highlight the corporate accounts business, where while that is the definition of streaky to your question because we meet large customers when they're ready, it's a very attractive piece of business that is that we are uniquely positioned to serve in the industry. So things like that happens tricky, things like [CNI] have been relatively consistent. So that builds us a strong foundation, so that we can adapt to where opportunity is in the market.

And then we'll continue to invest to add new areas of competition for the lighting business specifically, and we'll talk about spaces, I'm sure later. But there we talked about horticulture and petroleum. So the streaky places, as Karen identified was around corporate accounts, which is a very attractive piece of business for us.

Christopher Glynn Glynn - *Oppenheimer & Co. Inc. - Analyst*

Okay. Thank you.

Operator

Ryan Merkel, William Blair.

Ryan Merkel - *William Blair & Company L.L.C. - Analyst*

Hey, thanks for taking the questions. I wanted to ask as well on the order rate growth. Neil, can you just talk about which end markets you're seeing positive trends and maybe by geography where things are a bit stronger?

Neil Ashe - *Acuity Brands Inc - Chairman of the Board, President, Chief Executive Officer*

Yeah, I'll start and Karen add color as you see see fit. Let me first start by the disaggregated revenue. We've seen consistency in the C&I channel, as I said earlier. So that's our agent to project business throughout the country. And that has been stronger in areas where you expect like myself, areas where there are growth kind of in the country obviously, again. Strengthen and corporate accounts and the opportunities that we have there, longer term strength in our infrastructure.

So we are taking longer live orders, if you will. So that satisfy over a longer period of time time that we have in the past. So we've talked about the city of Philadelphia, Hall of Fame, for example. There are others that that look and smell and smell like that. So yes, I mean, it is not -- we are in a market where everything is up and to the right. But our diversity of opportunity is presenting us the ability to continue to have a relatively consistent order rate. Karen, anything you'd like to add?

Karen Holcom - *Acuity Brands Inc - Chief Financial Officer, Senior Vice President*

Yeah. The only thing I would like to add, Ryan, is that when we looked ahead, infrastructure continues to show positive signs. It's not landing yet, but the quoting activity is really strong. So as we look ahead, I think we have the portfolio that service that business and see it as an opportunity for us.

Ryan Merkel - *William Blair & Company L.L.C. - Analyst*

Got it. Okay. That's helpful. And then I wanted to go back to the comment you made about not shipping maybe as well as you could have and you're going to address that. Can you just talk about that? And then when do you think you'll solve that?

Neil Ashe - *Acuity Brands Inc - Chairman of the Board, President, Chief Executive Officer*

Yeah. So as we said, our orders exceeded our shipments, which means we generated backlog during the quarter. That backlog will be executed and shipped. And the reason is we didn't meet our daily production targets and there are a handful of reasons for that. None of which are alarming and we are in the process of addressing them all. So we'll sort those out and over the course of this quarter, in the next quarter, and we'll be back to where we want to be.

Ryan Merkel - *William Blair & Company L.L.C. - Analyst*

All right. Thanks. I'll pass it.

Neil Ashe - *Acuity Brands Inc - Chairman of the Board, President, Chief Executive Officer*

Thanks, Ryan.

Operator

Tim Wojs, Baird.

Tim Wojs - *Robert W. Baird & Co. Incorporated - Analyst*

Hey, everybody. Good morning. Just to start just on getting into kind of the refueling and kind of the C-store market. I guess maybe just if you could step back and kind of talk about maybe why Acuity didn't address that market in the first place? And how maybe the unit economics of that business and independent compare to kind of your existing portfolio?

Neil Ashe - *Acuity Brands Inc - Chairman of the Board, President, Chief Executive Officer*

Yeah. So it's a good question. So if you'll allow me, Tim, I'll just elevate for a second to say that, I think one of the perceptions in about Acuity Brands lighting and inclusive of our own is that because we're the largest in North America, we assume we're the largest in North America, which means we aren't always good at seeing the opportunities where we didn't compete.

So we are highly focused on where we do compete and we historically were less focused on where we didn't compete. So the refueling vertical, as an example of where we didn't compete, and so we paid some attention, but not enough attention to what that business was. And they were for any number of reasons focus. We had all other things to do, et cetera.

As we've focused the company now on finding these opportunities to grow where we are either not competing or not competing fulsomely, we've started to identify a rich niches where we want to and verticals where we want to go compete. The refueling one is an obvious one. So it's attractive for the size of the ultimate market at the end user base or an end basis, number one.

Number two, it's an attractive competitive market with effectively limited competitors. So we decided to enter that business organically because obviously we can create a ton of value by building an attractive sized business in that vertical.

So we invented new fixtures that support the core of that, which is canopy lighting. Those fixtures are at least as -- but in most cases, more competitive than what's currently in the marketplace. Those fixtures than pair with a lot of the rest of our portfolio to serve the rest of the facility. So imagine yourself on our EV charging lot or a gas station. And what that really is a canopy area and a facility where retail and food is sold, which obviously we excel in evidence our corporate accounts this quarter.

So when you put those two together, that creates an attractive market for us to go service. And I want to commend our teams for their ability to organically develop the product portfolio at a really rapid pace so that we can meet that market. So then we get to do other things we're really good at like go and recruit the top independent sales agent in that market to represent us. And so we're optimistic about our ability to do this in this vertical and for it to be a an attractive part of our portfolio going forward.

Tim Wojs - *Robert W. Baird & Co. Incorporated - Analyst*

Okay, great. And then maybe at a higher level question also, but on SG&A, we've seen that kind of right now to maybe 32% or so of sales. I know this year, it's been kind of a little walk in terms of the sales numbers. But I guess as you look out over the next couple of years, I mean, when would you expect to start to see leverage on the heightened SG&A expense?

Neil Ashe - *Acuity Brands Inc - Chairman of the Board, President, Chief Executive Officer*

So I'll start and then Karen will add actual real color to the conversation, but [specific] big picture on SG&A, I want to highlight it is SDNA. So there's their sales and marketing and then there's the distribution that is -- that we recognized in that number. So the distribution part of that is really part of our operations and we are addressing that going forward to improve that. But that currently generally moves basically in line with our volume.

So if we put that aside, then from an operating expense -- and then sales and marketing, obviously is driven by the largely by the commissions we pay to the independent sales network. Within operating expenses than our priority and where our investment has been, has been around technology. So we have historically been underinvested in technology and realized as a result not as many of the benefits as we could.

So our priority there on the investment is to drive technology, which is helping to deliver some of the gross margin performance and will ultimately be more leverageable going forward. Karen?

Karen Holcom - *Acuity Brands Inc - Chief Financial Officer, Senior Vice President*

The other thing, I would point out is that if you look at the dollar investment quarter-to-quarter and fiscal 2024, we've been pretty consistent. So as we look to return the business to growth, I think that's where it will have a real opportunity to leverage our current level of fixed investments.

Tim Wojs - *Robert W. Baird & Co. Incorporated - Analyst*

Okay, great. Thanks a lot.

Operator

Joe O'Dea, Wells Fargo.

Joe O'Dea - *Wells Fargo Securities, LLC - Analyst*

Hi, good morning. Thanks for taking my questions.

Neil Ashe - *Acuity Brands Inc - Chairman of the Board, President, Chief Executive Officer*

Good morning, Joe.

Joe O'Dea - *Wells Fargo Securities, LLC - Analyst*

I wanted to start on cash now at about \$700 million and just thinking about deployment opportunities, any color on the M&A pipeline and also the potential size of what's within that and the stocks now and then sort of double digits from highs earlier this year? So does that give you an opportunity to sort of reconsider deployment and think about reengaging on repo or more?

Karen Holcom - *Acuity Brands Inc - Chief Financial Officer, Senior Vice President*

Yeah, Joe, this is Karen, I'll start and then Neil can add more color on the M&A pipeline. Our free cash flow, we're really pleased with where we are year to date were \$404 million of free cash flow, and we continue to invest in the business.

So our first priority is always to invest in our current businesses as for growth, when you see us doing this through our product vitality efforts. I'm also pleased to announce new [Lansing] this unlinked then yesterday.

We read our Distech facility and we are expanding those operations both in Lyon and in Montreal to support the growth for that business. So that is our first priority is to invest our current businesses for growth.

Neil will talk more about the M&A pipeline. We did increase our dividend, if you recall this year. So our third priority is to increase our dividend. And for the first time in January, we increased it by 15% and maintain that level of dividend after this this quarter.

And then finally, share repurchases as you acknowledged. So we've said it before when our share price is high, we buy, less when our share price is low, we buy more. And we really have demonstrated that consistently over the past four years, allowing us to buy a significant amount of our shares back over that time.

So we would feel really good how we've allocated that capital today, Neil?

Neil Ashe - *Acuity Brands Inc - Chairman of the Board, President, Chief Executive Officer*

Yeah. So I'll emphasize a couple of things that Karen said, first is that we're investing for growth in our current businesses, evidence, horticulture, petroleum and the expansion at this tech, et cetera. So we were appropriately we recognize that -- we can create a ton of value with organic growth funded by our cash flow.

On the M&A, we recognize also that we can expand the portfolio and expand the company in the process. And so we have a robust pipeline of small and medium-sized acquisitions that fit very well with our strategy going forward. And our priority there is around the spaces business where you've seen us do things like term, there are more like that. There are opportunities for us to increase our addressable market and the things that we can control and the manner in which we can control them. And so we're working on that.

We also have of a developing strong pipeline in the lighting business as well, where we may have the opportunity to put capital work in an attractive ways. But again, we're disciplined. We -- what we look for one needs to align with our strategy. Two, we need to understand how we can integrate and on operate that. Three, we need to understand its impact on our business, our company and our financial performance. And then fourth, we have to have the opportunity to acquire it at the appropriate valuation.

So these things take time. I'd like to say, opportunity knocks, it doesn't come when it's called. So we will continue to prosecute those opportunities. But we feel really good about the pipeline and and where we could potentially be over the next couple of years.

Joe O'Dea - *Wells Fargo Securities, LLC - Analyst*

So helpful details. I appreciate it. And then just wanted to ask on sort of industry indicators versus demand trends you're seeing, I think headline figures seeing some softness in softer than expected. ABL revenue wasn't all that surprising when we look at ABI and Dodge Momentum. But it sounds like that was maybe more sort of internally related and the commentary on order activity is encouraging.

And so just when you're looking at those indicators and you're seeing the end market, what are the disconnects between the two such that the underlying demand that you're seeing in orders is still pretty healthy?

Neil Ashe - *Acuity Brands Inc - Chairman of the Board, President, Chief Executive Officer*

Yeah. I would say a couple things on that, Joe. So first is that we're the largest in the market. So obviously, we're going to be affected by the market. Our growth algorithm and straightforward. So the impact of the market, one. It's our ability to take share, two, and it's our ability to grow and things three. So you're seeing in some of that, we're really all three of those in our order rate.

The -- as we as we mentioned, we did build backlog during the quarter. So on a natural basis, sales could have been a little bit higher in this quarter, but those will be satisfied in the next quarter.

We -- as we've talked about a fair amount, we are as you know, I am data-focused. And so I'd prefer to talk about what we know versus what we think. So the regression work that we do on a consistent basis would demonstrate that we are outperforming what our historical performance would suggest that we would do. So that is the combination of all of that we done before. We have not been able to convincingly predict exactly where -- use an outside, specific single outside variable to consistently predict what the market will be.

So ABI, for example, is just one of the metrics that we use Dodge's. But one of the metrics there we use. When we consolidate those and we are we are -- we do this every month and we are and we iterate and we tried to make our model better and better and it is getting better. And the other takeaway is that we're outperforming what the data would suggest that, that we would do, which means that we're outperforming our both our past and the industry metrics.

Joe O'Dea - Wells Fargo Securities, LLC - Analyst

And then just one clarification related to the production that you talked about in the quarter, can you just size with their revenue impact is? And do you expect to fully capture that in the fourth quarter?

Neil Ashe - Acuity Brands Inc - Chairman of the Board, President, Chief Executive Officer

Yeah. So we've -- and we've talked about this during kind of the last couple of years as things have we saw around. We have orders, those turns into backlog, we produce that and then it shifts. So we don't have a phenomenon or orders are canceled.

So orders are orders for us. So it's just a matter of when we ship. The second thing I'd highlight is that we were focused on, as we've said, returning the lighting business to growth. That will happen in either this quarter, the next quarter based on how we trend that out.

So we like to focus on the longer term and our ability to grow this business. We're confident in our ability to continue to grow the lighting business. And we're confident in our operating performance and our ability to continue that as well.

Joe O'Dea - Wells Fargo Securities, LLC - Analyst

Got it. Thank you.

Operator

Jeffrey Sprague, Vertical Research Partners.

Jeffrey Sprague - Vertical Research Partners, LLC - Analyst

Thank you. Good morning, everyone. Just -- I want to come back to kind of the production just because -- it's actually a little surprising to hear it in an environment where demand is a particularly strong, right? It sounds like you're trying to ramp up to some higher level. And then here it's multiple things not like one thing perhaps like a supplier dropping the ball.

So can you give us a little bit more color on what happened? and sort of those said a little bit about quarter two, you get it cleaned up, but it just kind of sounds a bit surprising that this would have manifested across several different inputs.

Neil Ashe - *Acuity Brands Inc - Chairman of the Board, President, Chief Executive Officer*

Yeah, Jeff. First of all, I want to emphasize what I said, which is not alarming. And we have now developed the consistency of communication where we'll tell you exactly kind of what we're thinking about and we won't throw kind of either suppliers under the bus or not answered the question.

There is nothing alarming about this production. We had a -- the core issue is a mild labor. We didn't -- a labor issue, which is we didn't ramp up labor as fast as we needed to because we didn't think we would need to ramp it up that fast. We can solve that problem and relatively short order and solve that going forward.

So this is not as I said, there is nothing alarming about this -- and its impact going forward. So we feel really good. I will tell you a preview what our internal communication is, which we're sending out and about 30 minutes, which is that as we've improved our company, our expectations for our own performance are higher.

So we are holding ourselves to a higher standard and so I don't think many companies would have called out that we missed our production targets this quarter, but our expectations for our own performance are higher and so -- and our team's expectations for our performance are higher. So again, nothing alarming here. We will sort this out and and go forward.

Jeffrey Sprague - *Vertical Research Partners, LLC - Analyst*

And then on the other side of the equation, the other gross margins continue to look impressive, which I hear production problem, I think down gross margins up gross margins right at that one point into the discussion today is that design select us not the primary driver. Can you just maybe elaborate what -- you pointed to product vitality service levels and productivity? I mean, is that the order of magnitude, is there anything in particular that stands out on the gross margins? I know direct price discussion as a bit anathema, but maybe just talk about what's going on the price cost side in aggregate.

Neil Ashe - *Acuity Brands Inc - Chairman of the Board, President, Chief Executive Officer*

Yeah. So let's do spend a few minutes on this, Jeff. Thanks for for the question. So let me first start with product vitality, and I'll use the frame which we focused on as an example. That is and we've talked about several big fixture prop projects over the course of the last couple of years that have done something similar, which is -- we are delivering a higher value products to marketplace was significantly less content.

So as you saw in the images, this is literally a snap together fixture that replaces a panel and in the ceiling of an office or K [through] 12 school, for example. So they're significantly less content in that fixture. So obviously, our ability to drive margin with less material is much higher.

Second, I would say on the pricing front, we have been, as we've said, we've become very strategic about how we price. So, and our size strategy is very clear on the Contractor Select portfolio, which is 300 high-volume products, which are designed to be stocked and resold. We are we are very competitive from a price perspective, although not not the lowest price and we are the most competitive from a value perspective.

In other words, what you get for your money. So switchable technology and other things, we've created an opportunity for the end user to be able to trust those products in each of their projects. And we've created the opportunity for distributors to earn higher returns because when they focus on our products, they know that they don't have to carry as much inventory. They also don't have to carry as much exogenous inventory. In other words, inventory of other folks.

The third thing I'd highlight, which I addressed a little bit earlier in one of the questions was the now fully integrated performance of our [elderly] and OPTOTRONIC drivers. So by controlling the electronics in our luminaries in our controls, we have largely completed that vertical integration, which gives us a number of advantages among them as margin.

So and then finally, we continue to have opportunity to us to increase service levels and drive productivity. So as I mentioned earlier in the call, we're on a path here. We're not a destination and so -- and each one of those is working together. And the cumulative effect of that is what we think it's really good performance.

Jeffrey Sprague - *Vertical Research Partners, LLC - Analyst*

Great. Thanks for that. I'll leave it there.

Neil Ashe - *Acuity Brands Inc - Chairman of the Board, President, Chief Executive Officer*

Thanks, Jeff.

Operator

Thank you, I'm showing no further questions in queue at this time. I'd like to turn the call back to Neil Ashe for any closing remarks.

Neil Ashe - *Acuity Brands Inc - Chairman of the Board, President, Chief Executive Officer*

Thank you. We appreciate you all for joining us today. So as we've talked about consistently, we are focused on returning our Lighting -- Lighting control business to growth while we continue to drive margins and strong cash flow. We feel like our Spaces businesses' performance is impressive and growing and we have opportunities to continue to grow our portfolio over time.

So with that, we will get back to work and deliver on the fourth quarter and we'll talk to you soon. I hope you all have a good day.

Operator

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

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