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Market Intelligence

# **HNI Corporation** NYSE:HNI

## *Earnings Call*

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# Call Participants

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& CEO*

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*Senior VP & CFO*

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**Reuben Garner**

*The Benchmark Company, LLC,  
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**Steven Ramsey**

*Thompson Research Group, LLC*

# Presentation

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## Operator

Thank you for standing by. My name is Amy, and I will be your conference operator for today. At this time, I would like to welcome everyone to the HNI Corporation Third Quarter Fiscal 2024 Results Conference Call. [Operator Instructions] It is now my pleasure to turn the call over to Mr. McCall. Please go ahead.

## Matthew Schon McCall

*Vice President of Investor Relations & Corporate Development*

Good morning. My name is Matt McCall. I'm Vice President, Investor Relations and Corporate Development for HNI Corporation. Thank you for joining us to discuss our third quarter fiscal 2024 results. With me today are Jeff Lorenger, Chairman, President and CEO; Marshall Bridges, Senior Vice President and CFO; and VP Berger, Executive Vice President.

Copies of our financial news release and non-GAAP reconciliations are posted on our website. Statements made during this call that are not strictly historical facts are forward-looking statements, which are subject to known and unknown risks. Actual results could differ materially. The financial news release posted on our website includes additional factors that could affect actual results. The corporation assumes no obligation to update any forward-looking statements made during the call.

I'm now pleased to turn the call over to Jeff Lorenger. Jeff?

## Jeffrey D. Lorenger

*Chairman of the Board, President & CEO*

Good morning, and thank you for joining us. I'm going to divide my commentary today into 3 sections. I will start by providing some highlights on our third quarter results, which were strong. Non-GAAP EPS of \$1.03 exceeded our internal expectations and was 11% higher than the prior year period despite continued revenue pressure. Then I will discuss our expectations for the fourth quarter, where we expect the near-term demand pause to impact results.

Finally, I will cover why we are confident in our ability to continue to drive profit growth in the upcoming years. Specifically, I will highlight 3 key points that underscore our positive outlook for '25 and '26. We have elevated EPS visibility through 2026. Our workplace demand outlook remains encouraging, and our unique position and strong long-term market fundamentals provide reasons for optimism in Residential Building Products.

Following those highlights, Marshall will review our outlook and to discuss our strong financial position. I will conclude with some general closing comments before we open the call to your questions.

Let's start with the third quarter. Our members again delivered strong profit growth. Our 11% non-GAAP EPS growth in the third quarter was on top of a very strong year ago comparison, when profit grew more than 30% year-over-year. Third quarter EPS has more than doubled in the past 3 years, and we delivered those results without top line support.

In the Workplace Furnishings segment, our profit transformation plan and acceleration of KII synergies drove segment non-GAAP operating profit margin to a 20-year high for the third quarter. In Residential Building Products, despite ongoing housing market volatility, non-GAAP operating profit margin expanded year-over-year and exceeded 18% for only the third time in the third quarter.

Our strategies, our dedicated member-owners, our customer-first business model and our proven ability to manage through all parts of the economic cycle again helped deliver strong results.

Next, a few comments about the fourth quarter. We are optimistic about the opportunities that we see in both segments. However, in the very near term, we are seeing a pause in demand across our businesses. As a result, fourth quarter profit is expected to decline versus the same period of 2023. In Workplace Furnishings, we are seeing demand moderate with small- and medium-sized customers.

Within the SMB space, our transactional business has been particularly soft. As you may recall, our transactional business primarily flows through wholesalers and national supply dealers. This business can be volatile. The selling cycle is short. It typically involves smaller item purchases and historically has been very sensitive to changes in the economy and general business sentiment.

Currently, economic and election concerns have small business leaders increasingly hesitant about discretionary spending. Indicative of this sentiment is the September small business optimism survey. The monthly uncertainty index hit a record high ahead of the U.S. elections. We expect business leaders' hesitation to moderate as we move past the elections and into next year.

In the contract furniture space, we are seeing further project delays and continued lengthening of the selling cycle. Encouragingly, activity and dealer sentiment are improving. However, customers are still being cautious, and our fourth quarter shipments will be negatively impacted.

A recent Deloitte survey illustrates these concerns. Of 130 large company CFOs that were surveyed, only 12% said now is a good time to take greater risks. This is the lowest level in the past 10 years, even lower than the worst stages of the pandemic. But again, we view these pressures as temporary.

Finally, in the Residential Building Products segment, during the quarter, builder and homeowner sentiment was negatively impacted by interest rate volatility, ongoing inflation and affordability issues and the same economic and political uncertainty that is impacting our Workplace business.

Reflecting these concerns, the Housing Market Index fell to 39 in August after reaching a peak of 51 in March and April. As 2025 develops, we do expect interest rate reductions to eventually result in increasing housing turnover and improved demand for our products in both new construction and R&R.

Moving to my first point, highlighting our optimism beyond the fourth quarter. We have 2 initiatives underway: Mexico and KII synergies, that by themselves will deliver \$0.70 to \$0.80 of EPS growth in 2025 and 2026. That represents approximately 25% of EPS growth on top of our already-strong results.

Even with the slower fourth quarter, we expect to generate record non-GAAP EPS in 2024, which will be our third consecutive year of double-digit non-GAAP EPS growth. This means that without help from the cycle, we expect our 3-year double-digit earnings growth streak to extend through at least 2026.

Remember, our Workplace Furnishings profit transformation plan does not require revenue growth, and our recent margin expansion has been achieved without cyclical top line support. In addition, we continue to adjust our cost structure in Residential Building Products to align with the current demand environment.

Early in the fourth quarter, we took actions that will lower our cost structure by approximately \$5 million in Residential Building Products. Most of that benefit will be recognized in 2025, further adding to our profit visibility. Before moving to my second point, I'll cover a few additional comments on KII and the recognition of synergies.

KII continues to be highly accretive and was a major contributor to our strong third quarter profit, and total synergies expected to result from the Kimball International acquisition have increased another \$10 million and now are expected to total \$60 million, with \$30 million to be realized in '25 and '26. KII is also providing us with new revenue growth opportunities and is highly complementary.

Kimball International's workplace offering improves our post-pandemic product and geographic positioning, and KII's hospitality and health care businesses are well positioned within attractive expanding segments, and both are generating growth. Our confidence in the combination of strategic and financial benefits continues to prove out and accelerate.

Moving to my second point supporting our optimism. The outlook for Workplace Furnishings demand remains encouraging. Segment orders have continued to improve early in the fourth quarter after growing 1% in the third quarter. I'll now comment on the order trends of SMB and contracts separately.

Our SMB activity moderated in the quarter, consistent with small business sentiment trends and our exposure to transactional business. SMB orders declined 3% year-over-year in the third quarter against a

challenging comp. In the third quarter of 2023, SMB orders grew 6% year-over-year. As you may recall, SMB has been an area of strength for us for some time.

This segment of our business has generated consistent order growth over the past 2 years, and we remain bullish about the fundamental backdrop. Specifically, healthy dynamics, including population shifts to secondary and tertiary geographies and relatively higher office usage in those markets point to a return to growth in 2025.

In our core contract business, we see growth on the horizon. The combination of contract and KII orders were up 5% on a year-over-year basis in the third quarter. We have seen large projects reactivate and continued strength in the hospitality space. As a result, orders over the past 2 months have improved. However, most of these projects will ship next year.

Further supporting our outlook, quarter-ending workplace backlog is up 5% versus the prior year. Additionally, our contract sales funnel for 2025 continues to be encouraging and is up over 10% year-over-year. Looking out, we believe we are particularly well positioned to benefit as the Workplace Furnishings market continues to improve.

We have unmatched product and pricing breadth and depth. We have products that work for customers, ranging from small businesses to the largest multinationals. Our brands are distributed widely across geographies from tertiary markets to the top MSAs. And we can broadly meet the needs of workplaces, schools, health care facilities and hotels.

Moving to my third reason for optimism. We continue to see positive long-term market fundamentals in Residential Building Products. Single-family housing remains undersupplied, and demographics will support additional demand growth.

Over the next year, we expect these fundamentals, combined with anticipated interest rate reductions, to eventually flow through, driving increased housing turnover and improved demand for our products in both the new construction and R&R spaces.

In addition to the strong market fundamentals, we continue to invest in unique growth opportunities. These include new product innovations such as electric fireplaces, efforts to become more intimate with builders, homeowners and homebuyers, online capabilities and the expansion of our wholly-owned installing distributor footprint.

I will now turn the call over to Marshall to discuss our outlook for 2024. Marshall?

**Marshall H. Bridges**

*Senior VP & CFO*

Thanks, Jeff. I'll start by summarizing our outlook for demand and profit, beginning with demand. Fourth quarter revenue in Workplace Furnishings is expected to decline at a low- to mid-single-digit rate year-over-year. Our new outlook represents a reduction from what we provided in our July earnings release, which implied fourth quarter growth.

Moving to Residential Building Products. We expect fourth quarter revenue to decrease at a low single-digit pace versus the same period in 2023. This is also down from our prior outlook, which anticipated growth in the fourth quarter.

Shifting to our profit outlook. We expect margins in Workplace Furnishings to move modestly lower year-over-year, driven by lower volume. Margins in Residential Building Products are expected to be mostly unchanged to down slightly. In total, fourth quarter earnings are expected to decline year-over-year. Despite that decline, we expect full year EPS to increase and extend our streak of growing full year EPS by 10% or more to 3 years.

I'll wrap up with a few comments on our balance sheet. We improved our already-strong financial position. Gross leverage at the end of the quarter was 1.1x as calculated in accordance with our debt agreements. That ratio was down from 1.5x at the end of the second quarter due to higher profit and lower debt levels.

I would also like to point out that we are very near the same leverage ratio that we had before the Kimball International acquisition, so it took us just over 5 quarters to delever, which is a testament to our ability to consistently generate strong free cash flow.

During the quarter, we also accelerated our share repurchase activity with more than \$11 million of buybacks. The combination of our strong balance sheet and consistent cash flow generation provides a high degree of financial flexibility and capacity for capital deployment. Our current priorities for cash deployment remain reinvesting in the business, funding dividends and pursuing share buybacks and M&A opportunities.

I'll now turn the call back over to Jeff.

**Jeffrey D. Lorenger**

*Chairman of the Board, President & CEO*

Thanks, Marshall. We remain committed to expanding margins in Workplace Furnishings and driving long-term revenue growth in Residential Building Products. We drove strong results through the first 3 quarters of 2024, delivering year-to-date earnings growth of 33%, and we anticipate record EPS for the full year. Beyond this year, we are positioned for continued success.

In summary, we have elevated earnings visibility in '25 and '26, broad and diverse product and market coverage in Workplace Furnishings and market-leading positions in Residential Building Products, all supported by our strong balance sheet and the ability to drive continued free cash flow. I want to thank each HNI member for their continued dedication and congratulate them on delivering another quarter of excellent results.

Before we take your questions, today will be Marshall's last earnings call as CFO. Marshall joined HNI 23 years ago, and he and I have worked side-by-side now for close to 15 years. On behalf of the Board of Directors and the entire HNI team, I want to thank Marshall for his many contributions to the corporation through the years. While Marshall will no longer be our CFO, we are happy he will continue to be part of HNI, and will be working in a part-time role assisting with strategic projects focused on artificial intelligence.

VP Berger, who is on the call with us today, will be taking over as CFO at year-end. VP led our Residential Building Products business for the last 9 years and has been part of the organization for 27 years, serving in various financial, operational and leadership roles. We are fortunate to have VP ready to step into the role and expect a seamless transition. Thank you again, Marshall. Good luck in semi retirement. We will now open the call to your questions.

## Question and Answer

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### Operator

[Operator Instructions] Your first question comes from the line of Reuben Garner with Benchmark.

### Reuben Garner

*The Benchmark Company, LLC, Research Division*

Congrats, Marshall and VP. I look forward to working with you. So let's see. Where should we start? The Residential Building Products' near-term kind of softness that you're seeing, can you go into a little more detail there, what exactly you're seeing?

Is it more new construction slowdown we saw over the summer kind of hitting you guys now? Is it more on the R&R side, just continued with rates being elevated? And then any signs of further destocking? I know last year, there was -- it's not a heavily inventoried product. But last year, there was a bit of a reset to normalize. Any signals that there's more of that, by chance?

### Jeffrey D. Lorenger

*Chairman of the Board, President & CEO*

Yes, Reuben, I think -- and this is a piece. Our outlook, it really falls into 3 equal weighted pieces, and you're asking about one of them, of reduction in near-term demand. And it's really in our stove business, which is a large part of our remodel/retrofit business. I think I'll let VP provide some color on what's happening with stoves.

### Vincent Paul Berger

*Executive VP and President of Hearth & Home Technologies*

Sure. Reuben, I think we start with the business itself. It's a short cycle purchase. Anything like that provides obviously low visibility. But historically, the band for this business has been pretty predictable outside of extreme oil prices or then obviously the pandemic. So as we firmed up thinking through the second half, we did expect this to stabilize.

And with stabilizing, it actually would show some pretty strong growth in the fourth quarter year-over-year because of how we finished in 2023. As you recall, the prior year comps were pretty low. Backlog was starting to deteriorate and come down. And as we thought the inventory destocking that was happening across the business went through, we would favorably see that in the back half of this year.

So all of that's happening. It's just normalizing a little bit slower than we thought. And as we unpack it, whether it's the economy, warm weather, it's certainly dependent upon this business with the products and even the election. So I would say it's all kind of playing out as we thought, just a little slower than we thought.

But also on the new construction side, not just the stoves, we are seeing some growth. It's just growing slower than we thought. We came into this plan, thinking about the third quarter, shooting for a 4% growth. It actually came in at 2%. So that's encouraging, that we're actually seeing some activity there.

But fundamentals haven't changed. And as we go into the fourth quarter, we see that this has continued to be an area for us to grow, just probably not at the same pace as we are right now. So the reason for that is really about home buying conditions. They haven't improved to the point where we thought they would, although there are things that, to Jeff's point, that's why we believe that we should know that optimism there as we go forward.

### Reuben Garner

*The Benchmark Company, LLC, Research Division*



And so would you -- I know you're not providing '25 guidance yet, but would you expect that this softness might persist into the early part of next year until we can get to kind of the spring building season and see where rates and the builders and the consumer lands at that time?

**Marshall H. Bridges**

*Senior VP & CFO*

Yes, Reuben, I don't -- we don't see something that's going to change the conditions radically from where we are right now. I think it's a bit premature to project anything in 2025, given all the uncertainty that we're facing here in the upcoming weeks. But I think that's a pretty good assessment.

**Jeffrey D. Lorenger**

*Chairman of the Board, President & CEO*

Agree.

**Reuben Garner**

*The Benchmark Company, LLC, Research Division*

Okay. And then on the Workplace side, and forgive me for the near-term questions, but these are the 2 kind of items that seem to have changed this quarter.

The transactional business versus the order trends you're seeing, is that dichotomy something you've seen before? Does transactional typically lead the orders and maybe, therefore, you're anticipating some negative order growth in the fourth quarter? Just walk me through how those 2 relate historically.

**Jeffrey D. Lorenger**

*Chairman of the Board, President & CEO*

Yes, Reuben. I think that's a good point. Just to level set, we're seeing -- basically, why has the outlook for fourth quarter changed? And it's really -- I want to start with -- we've -- before I get into those details, we continue to drive profit growth without top line support. So I think we're really -- as I said in my prepared remarks, '25 and '26, we have a lot of visibility to, and we've shared those numbers.

Shifting to your question, there's 3 areas. We've just commented on one of them. They're probably equally weighted in the fourth quarter, and the transactional businesses represents about 1/3 of that weighting. And you're right. This is -- this business flows through wholesalers and national supply dealers.

It's roughly 20% of our SMB sales, but it can be volatile. It's more discretionary purchases, it's much more short cycle. And historically, it remains -- historically has been and still remains sensitive to changes in the economy. So we don't see that as a growth driver. We do think it will stabilize, but it is the piece that is really leading the short-cycle stuff right now.

And it's economic driven. We've seen this in the past. Whether it's indicative right now of anything else, I think there's enough dynamics in the economy that I wouldn't say it's a leader or a lagger. It's really, we believe, more of a temporary kind of economic short-term election cycle, what's going to happen, and it's more reflective of that than it is a lead or lag situation.

And the second area I should comment on is -- the other third weighting in the change in our outlook is the contract business. And as I -- we continue to see solid indications of growth, the timing of shipments and orders continue to push out.

So what we're seeing currently is our sales funnel is up 10%, more than 10%. The dealers are increasingly confident. Our order trends are improving. The combination of North American contracting KII orders was up 5% in the third quarter, and the return-to-office efforts continue to ramp up across most large MSAs. Lease churn continues to accelerate as tenants take advantage of lease economics and nonviable spaces kind of coming off the market.

So however, the activity is predominantly landing in '25 due to customer requests. So on the positive side, longer timing is driving an increase in backlog. So our backlog is up 5% year-over-year, giving us better visibility to next year. But what we have seen with this lengthening -- and we've talked about this for a



couple of quarters now. So let me provide a couple more comments and a bit more color on this, this dynamic of order-to-ship dynamic.

There are multiple drivers that we are seeing when we talk to customers. Customers are still sorting through complex and dynamic real estate and return-to-office decisions. They're wrestling with many factors as they attempt to figure out the most productive floor plates that support their return-to-office initiatives. And candidly, there's more decision-makers in the process than there historically has been. And so customers are asking for more data to facilitate decision-making.

So all that lengthens this sales process. The other thing that's going on is inflation has challenged some of the budgeting, and by the time the furniture is getting specced, budget challenges drive additional design iterations as customers do more value engineering, which, by the way, is good for us given our breadth and depth of price points and product coverages.

So then the final dynamic there on this lengthening order-to-ship is they remember the disruptions caused by supply chain issues, and so when they finally order, they're ordering earlier, extending times between order and install.

So all this results in more specs, more design iterations, extended sales cycles. And then finally, this economy election timing is kind of adding to the delay. So that's really what's going on. I wanted to take a minute and kind of give you a view on what we mean and what's behind kind of the dynamics of the expanding cycle.

#### **Operator**

The next question comes from the line of Greg Burns with Sidoti.

#### **Gregory John Burns**

*Sidoti & Company, LLC*

With the leverage now back down to, I guess, pre-Kimball levels, how should we think about maybe your capital allocation priorities? Are acquisitions now a consideration again? And it seems like you're buying back stock here also. Maybe you can just talk about, just generally, how you think about the balance sheet, leveraging that, and using that to maybe grow inorganically?

#### **Marshall H. Bridges**

*Senior VP & CFO*

Yes, Greg. As I mentioned in our prepared remarks, we're going to generate some strong free cash flow this year. We expect free cash flow to be somewhere in the \$180 million to \$185 million range for the year, which is above \$3.75 a share. So I just point out that, that's a strong level in excess of net income.

Now what to do with it? We remain committed to reinvesting in the business, of course. The dividend is important to us. And then after that, we continue to assess share repurchase and M&A opportunities on a case-by-case basis. We have been ramping up our share repurchases and anticipate continuing to do that. There's really not a need to delever from here. We feel very comfortable with the leverage we have.

#### **Gregory John Burns**

*Sidoti & Company, LLC*

Okay. And you talked about the revenue visibility, highlighting Mexico and Kimball synergies. I know you typically, on a year-to-year basis, have your ongoing profit initiatives. Like is there anything you could -- any maybe color you could add in terms of maybe next year or how that might contribute to profit growth next year?

#### **Marshall H. Bridges**

*Senior VP & CFO*

If you look at our history, we typically generate something like \$10 million to \$12 million of year-over-year profit benefit from productivity initiatives. Now I'm not sure what that means for next year, Greg, because we have a lot going on.

We've got the Mexico ramp up, we're finishing off the Hickory consolidation. So we're going to have some of our resources in executing those initiatives, but we would expect to generate year-over-year productivity regardless. And I think that we would be able to expand margins in '25 and '26 through the 2 initiatives Jeff mentioned earlier, as well as productivity benefits.

**Gregory John Burns**

*Sidoti & Company, LLC*

Okay. And in terms of the -- maybe both segments. First, on the office segment. Do you have a goal in mind in terms of where you think you can get those margins, given the profit improvement initiatives you have in place? And then maybe with maybe a little bit of volume help?

And then similarly, on the Building Products segment, I know you're taking out some costs here. Do you have a goal in mind or a level in mind of where you target operating that business regardless of where volumes maybe shake out for next year?

**Jeffrey D. Lorenger**

*Chairman of the Board, President & CEO*

Well, Greg, it's a good question. I think we are going to continue, as you just talked about, to expand margins and drive profit growth. So in the near term, we're going to continue to see this benefit. We have momentum. I'll point out that our operating margin in Workplace Furnishings is now over 9.5% when looking at our last 4 quarters.

So you combine that with more visibility to margin expansion in the upcoming quarters and years, it's going to drive record EPS this year, and then that's going to add strong free cash flow for next year. The target is -- I think if you just do the math, the \$45 million to \$50 million of synergies in our Mexico facility ramp, when fully operational, will drive an additional or approximately 250 bps of margin expansion in Workplace Furnishings.

That would put Workplace Furnishings operating margin near 12% in 2026 without the benefit of other initiatives, which we will continue to do, as Marshall just referenced. So consolidated EBIT margin would be over 10%. So that would be our expectation.

**Operator**

Your next question comes from the line of Steven Ramsey with Thompson Research Group.

**Steven Ramsey**

*Thompson Research Group, LLC*

I wanted to think about Workplace, and appreciate all the color on the lengthened time lines there. As you look forward and get past this near-term pause, is there any key cause that you think would recompress the time line? Or is this just kind of a state of business that you expect lasts even through 2025?

**Jeffrey D. Lorenger**

*Chairman of the Board, President & CEO*

That's a good question, Steven. I mean I think this initial wave of activity will probably kind of stay in this lengthened cycle until people kind of run a project through, and then we may start to see it return. But it's pretty dynamic right now, and I think it's more near term. And in most of next year, we think the cycle will remain lengthened.

Now having said that, like I said, we see demand activity that will go into the funnel that should add to this, and then you just have to tune your business to the length and cycle. We see that a little bit in the homebuilding side, with permits and how long it takes to build houses. That's recently lengthened out from 7 months to 9 months.

So it's really about predicting the rhythm of the business and getting it right and watching the funnel activity. But whether it returns to where it was pre-pandemic or even a couple of years ago, it's tough to say. I don't think it will immediately in the near term.

**Steven Ramsey***Thompson Research Group, LLC*

Okay. Okay. Helpful. And then thinking about Workplace, if there's a way to parse it out between office and non-office demand, and you alluded to some of this in hospitality, but thinking about non-office demand, is the sentiment and activity between office and non-office demand moving in tandem with one another? Or is there any notable divergence maybe near term, and then how you see it evolving kind of post this year?

**Jeffrey D. Lorenger***Chairman of the Board, President & CEO*

Yes. I think this year, if you -- the look back, I think you could say that there's been some verticals, education comes to mind, health care comes to mind. Even some of the state and local has been running a little ahead of general office. I think, with the demand metrics we're seeing on the horizon, that those things could probably more converge in a positive manner.

Now having said that, some of these verticals, education continues to be pretty strong. Health care continues to be pretty strong. But I think they'll come closer together, Steven, is the way I'd think about it, but there's probably going to be some frontrunners there. And I don't think office will probably lead it, but I think office will probably catch up to what some of these other verticals have been as we head into next year.

**Steven Ramsey***Thompson Research Group, LLC*

Okay. Helpful. And then last one for me. I know it's maybe too early to talk about the sales outlook for 2025, and clearly, volumes matter on this question. But I'm thinking about cash flow generation. You've got the operational moves to raise margins. With the plant and the shifting of operations, how do we think about the working capital impact and the CapEx needs for 2025? Just trying to, in order of magnitude, maybe think about cash generation next year.

**Marshall H. Bridges***Senior VP & CFO*

Yes. Working capital is pretty well normalized at this point. If you look at -- sequentially, we improved working capital, but we're pretty similar to where we were last year. Remember last year, we freed up over \$70 million in working capital. So we're not anticipating any kind of working capital usage on a year-over-year basis. And of course, we'll have the seasonal fluctuation.

CapEx this year, we're running a little bit below what we had planned. So in that \$180 million to \$185 million of free cash flow we expect to generate this year, that includes about \$65 million of CapEx. I would expect that to go up a bit next year as we kind of catch up to the projects we've been working on and finish out the operational moves that we've talked about before. But still think we're going to have a healthy level of free cash flow next year, and plenty of cash to deploy in a positive way.

**Operator**

The next question comes from the line of Brian Gordon with Water Tower Research.

**Brian Gordon***Water Tower Research LLC*

I just want to follow up on the last set of questions. Looking out kind of towards the intermediate to the longer term, how should we think about Workplace Furnishings, the breakdown of the business between the SMB, the contract and the other categories, the government, the hospitality, the health care?

**Jeffrey D. Lorenger***Chairman of the Board, President & CEO*

Are you talking kind of demand patterns or..

**Brian Gordon***Water Tower Research LLC*

Just sort of overall percentage of the business.

**Marshall H. Bridges***Senior VP & CFO*

We're a little higher in contract KII versus SMB. So I think as you look forward, the growth rates in those are going to move around depending on conditions. What we're seeing in the near term is that the contract business is showing a lot of strength. We're expecting that -- we're seeing a lot of that order pattern trend upwards and reflects kind of all these return to office mandates that we're seeing lease churn, et cetera, that we mentioned earlier.

So I think you've got some strength in the near term from that. And I think SMB, we feel well positioned there. We still have some population migration going on, so really well positioned to take advantage of the strength there. Now in the short term, we've got this transactional headwind that we discussed. But I think it's a little premature to call a major mix shift between those businesses. I think we're going to benefit as the market recovers and from our own unique initiatives as well.

**Brian Gordon***Water Tower Research LLC*

Okay. I mean, that definitely makes sense. When you were looking at the contract business specifically within Workplace Furnishings, any sort of breakdown between the projects that clients are coming to you about between greenfield and maybe kind of more refurbishment for getting people back to office or work from home?

**Jeffrey D. Lorenger***Chairman of the Board, President & CEO*

I think we're seeing activity, pretty healthy activity, in both buckets. You've got the lease churn that we talked about, people moving up in class of building, and that kind of becomes a greenfield. But you've got a lot of people who have campuses and are set in place, and they are looking at how do they redo that campus or redo a building of the campus and trial it out. We're seeing a lot of trial -- experimentation, so to speak.

So I think it's both. I think that people on return to office, whether they have a lease event that drives something, they're active because of the lease, we've always talked about a furniture event, and then they go into the return to office dynamics, and others are just trying to figure out how to make the office more productive in the hybrid work environment as they age in place, so to speak.

**Operator**

At this time, there are no further questions. I would like to turn the call back over to Mr. Lorenger. Please go ahead.

**Jeffrey D. Lorenger***Chairman of the Board, President & CEO*

Thank you. Before we end the call, this summer, we lost a long-time analyst and friend. Budd Bugatch passed away unexpectedly in August. For many decades, Budd was a great supporter of HNI and our industry in general. He was an outstanding analyst, mentor and friend. He was supportive, but also unafraid to challenge. And he earned the respect of those lucky enough to know him. Budd will be severely missed.

Thank you for joining us today. Have a great day.

**Operator**

This concludes today's conference call. You may now disconnect.

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