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Masco Corp. (MAS)

UBS Global Industrials and Transportation Conference - Fireside Chat

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CORPORATE PARTICIPANTS

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

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John Lovallo
Analyst, UBS Securities LLC

MANAGEMENT DISCUSSION SECTION

John Lovallo
Analyst, UBS Securities LLC

Okay, everybody, thanks for joining us. We appreciate you being here at the 2023 UBS Global Industrials and Transportation Conference. My name is John Lovallo. I'm the senior US homebuilding and building products equity research analyst here at UBS. So we're very excited to have Masco with us. Keith Allman, President and CEO, will open up by giving a few prepared remarks, and then we'll get into some Q&A. I'm sure most of you are familiar or very familiar with Masco, one of the largest manufacturers of both architectural coatings and plumbing products, big brands like Behr, Delta, Peerless, Brizo, Hansgrohe, just to name a few. So, very well positioned, one of our top picks this year.

With that, I will turn it over to Keith.

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

[audio gap] (00:00:54) here. I'm seeing some familiar faces and some maybe – some new faces that potentially are new to the story. So maybe I'll just indulge maybe with a little bit of a brief history of Masco for those of you that are new to it. Masco was founded in 1926 by a fellow named Alex Manoogian, who was an Armenian immigrant who came to the United States in search of better living possibilities for his family. He immigrated right here in Ellis Island and then made his way to Detroit, and two of his friends and business partners bought three dilapidated machine tools that didn't work. He fixed them up, got them to work, and started making car parts for Henry Ford's auto industry.

It was Manoogian, Adjemian and [indiscernible] (00:01:44), M-A-S Company. That's Masco. They started in 1926 and eight months later, the Great Depression just wiped out the US economy. And [indiscernible] (00:01:57) had families and they had to go do what they could to put food on the table and Alex Manoogian was there by himself. He hadn't brought his family over yet. And he kept it going, sleeping in the shop, living in the shop and making car parts and kept the business alive.

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In 1963, our company was doing $2 million in car parts in revenue and $2 million in this new innovation called the single-handle Delta Faucet. And at that point, he threw the keys to the company, to his son, Richard Manoogian, so that Alex could focus on philanthropy. And Richard was our second CEO, and he ran the company for 45 years and grew it from $4 million in revenue to $12 billion. I'm the fourth CEO in our company's 97-year history, and I've been in this role for just under a decade. It'll be 10 years here in a couple of months. So, that's the history of Masco. And thank you for indulging me. We're proud of that.

In terms of where we are today as you look on the slide, we're doing $8.7 billion in revenue, $600 million in adjusted free cash flow. And we have roughly 40 factories around the world with about 20,000 employees. Margin of 15.6%. And by the way, these are all 2022 actual numbers. We have two segments in our portfolio, Plumbing and Decorative Architectural. You see the numbers there in terms of revenue, about $5.3 billion in net sales in Plumbing and $3.4 billion in net sales in Decorative Architectural. And you see the margins numbers there as well.

To go into a little bit deeper dive into the individual segments, our Plumbing products is made up of some powerful brands, both in decorative as well as behind the wall and underneath the countertop in terms of rough plumbing, strong brand recognition, brands like Delta Faucet, Hot Spring Spa, Hansgrohe over in Europe.

We're roughly 80% North American, 20% International. And you see our distribution in terms of channel mix, about half of our products go through wholesale trade and the other half is divided into e-commerce, retail and specialty dealers, primarily our spa business. Solid track record of innovation. You see us with Touch2O, you see us with water conservation innovations. We run the gamut. Numerous growth opportunities and opportunities to grow both domestically as well as in Europe and internationally.

In our Decorative Architectural products segment, you see in the chart here, a little bit more detail, Behr Paint, one of the best, if not the best brands with regards to brand equity, brand awareness, service quality with the top five spots in an independently-rated magazine that rates quality.

A 40-year relationship with Home Depot. We've grown up with Home Depot. We were selling Home Depot paint when there was two Home Depot stores. And we have had an outstanding relationship and continue to have an outstanding relationship with Home Depot. Expertise in category management. And you can see principally a North American business through 97% in repair and remodeling.

In terms of our portfolio, we've made some pretty significant changes over the last decade with regards to how we're positioned in our businesses in the portfolio. By design, we have translated our portfolio to be lower ticket repair and remodeling, about 90% repair and remodeling. High margin, high cash flow business. We've done this to reduce the cyclicality and to improve the resilience of our portfolio. And this portfolio makeup, together with our execution, gives us the confidence to shoot for double-digit EPS growth through the cycles.

Strong cash flow, low CapEx, solid working capital management. So, that's a quick review of the business. And I think at this point, we're going to sit down and have a little conversation and do some Q&A.

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QUESTION AND ANSWER SECTION

John Lovallo
Analyst, UBS Securities LLC

Q

That sounds good. That sounds good. Great introduction. We appreciate it. Maybe starting from a really high level here, Keith, when – since you came on board, there's been a number of strategic portfolio decisions that were made in the installation business for TopBuild in 2014, Windows and Doors in 2019. Cabinetry business shortly thereafter.

When you look at the portfolio today, is this the right portfolio? And if not, what do you – how do you see it evolving?

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

A

We have confidence in our portfolio and its design and we've worked by design to get it to the position where it is today. As I mentioned in my earlier remarks, we believe that for the investor that is looking for a play in housing, but has the stability and the ability to weather these cycles and continuously deliver double-digit EPS growth through cycles, this portfolio is in good shape.

They're high margin businesses, they're low ticket R&R. So, for a high leverage bang for the buck, if you will, in terms of the difference you can make in a home with our products, paint, light fixtures, faucet fixtures, we play very solidly in a small, light touch remodel and then, of course, in the bigger ticket remodels, if you're doing a full-on bathroom remodel or kitchen remodel, you're not going to put an old faucet back on your countertop, and you're going to paint. So, we are agnostic to large ticket, small ticket swings, and that gives us the robustness and together with the solid cash flow to be confident in our return and our delivering of double-digit EPS through cycles.

Now, having said that, as you mentioned, we've – our board and management has a demonstrated track record of capability – and willingness and capability to execute on portfolio reconfiguration to drive shareholder value and that is a consistent reoccurring process that we have with the board to review potential for that. And that's going to continue.

John Lovallo
Analyst, UBS Securities LLC

Q

Makes sense. Okay. So then, if we maybe take that one step further and look at the current portfolio, what do you view as sort of the key synergies? You talked about small ticket R&R, but are there other things that tie this sort of Decorative Architectural and Plumbing portfolio together?

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

A

Yeah, John. Well, for starters, they're very similar businesses in terms of performance. They're high margin. They're relatively light CapEx and we have solid working capital management, strong cash flow. They are smaller ticket R&R focused. Our portfolio together is roughly 90% R&R and both of our segments are very close in that regard. So, they're well-matched. They match together.

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From a top line perspective, we share deeply between the two segments, our channel, go-to-market channels and the expertise that comes with that. So, we leverage customer and consumer insights into top line growth, and that's a fundamental synergy that we have. And the bottom line, of course, the scale and the diversification of the cash flow. So, in our view, these businesses are more valuable to the shareholder together than they are apart. And again, as I said, John, in your prior question, we have a regular board and management together process to review portfolios, we've executed on those in the past, and that process is ongoing and consistent. It's part of how we run the business and that's going to continue.

John Lovallo
Analyst, UBS Securities LLC

Q

Makes sense. Okay. Let's talk about Plumbing for a moment. There's been a lot of technology that's been infused in this business over the past maybe decade, but even over the past five years. Where do you see this industry going in terms of technology? I mean, touchless is something that's very important now. But where do you – what's the next thing for this industry?

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

A

Yeah. Our view on innovation is that the real value and the importance of how we drive with our productions, our manufacturing system and our innovation system is to begin with the consumer and consumer back. It's not something that comes out of our lab and then we try to push it or sell it. So I think the fundamental answer to your question is what is important to the consumer and to society as it relates to plumbing, and how does that inform where innovation goes.

And for us, a real significant component of it is water is a scarce resource. And water conservation and the ability to innovate sustainable products. And we have – we're doing a very good job with that, with roughly 40% of our products in that sustainable realm. And our innovation pipeline continues to drive that. So, [ph] I'd see water as (00:11:51) a scarce resource, is the main driver of and focus of innovation going forward in Plumbing.

John Lovallo
Analyst, UBS Securities LLC

Q

Okay. That's helpful. What if we took that same question maybe a little bit more challenging, but on the paint side. What – where's the market going for paint? What is the consumer sort of demanding or wanting there?

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

A

More of the same. Certainly environmentally sustainable, low VOCs. The environment is extremely important to our consumer and we need to be there. Beyond that, as we think about coatings and where we bring value and leverage with our partner, the Home Depot is what that consumer needs and whether that's coatings that can go on different surfaces more effectively and easier to apply, whether there's innovation to be had around coatings that can be put on and dry more effectively and quicker so that you need less of a window of, say, non-humid weather to be able to do the application. Whatever it is that the Home Depot consumer desires, that's where we're innovating.

John Lovallo
Analyst, UBS Securities LLC

Q

Okay. Makes sense. And then maybe let's zero in on Watkins for a moment. Really high-quality portfolio of product there. If we think about themes that are likely to kind of resonate into the future and wellness is something

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that seems like it's incredibly important. And what do you see as the biggest drivers of that business? I mean, is it wellness or is it something else?

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

A

Watkins is our spa business that we've had in our portfolio for quite some time. While clearly the focus of the majority of our product is in smaller ticket repair and remodel, to deliver that consistent performance that I've talked about and to drive us into a position for the investor that we want to attract, we like spas even though it's a big ticket because of which fundamentally what you mentioned, which we see as a strong tailwind for this space, mental and physical wellbeing and wellness is a trend that is driving our country and we're in Europe as well. We are the global leader in this position, and we think it's fundamentally important and one of the reasons we like this business so much.

And when you look at our performance in this portfolio and you go back to pre-pandemic, there was, obviously, a nice infusion of demand during the pandemic for these types of things, things related to home, to outdoor living.

But if you take 2019 levels and you put on a traditional growth rate of that, we're in excess right now. Even with a reduction in our volume from that peak of last year, we're still in excess of that track record, if you will, or that trend line from 2019 now. And we believe that is because of the health and wellness dynamic.

John Lovallo
Analyst, UBS Securities LLC

Q

Okay. Helpful. Maybe on Kichler, the acquisition that was made in 2018, lighting acquisition, challenging timing just given the Chinese tariffs came in shortly thereafter. When you think about Kichler, has Masco achieved what it set out to in the initial phases at this point or is there still sort of more work to be done there?

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

A

Yeah, the timing and when the tariffs came through, that was a challenge. There was also a significant challenge in the customer that chose to go in a different direction with regards to own brand. So, it was a challenging start to that acquisition. So no, we have not delivered on the investment thesis that we set out to deliver on. However, we've made significant structural costs reductions and improvements. We've completely revamped our supply chain where we procure products and our product development cycle. We have a new management team down there that's dynamic and doing a fantastic job. So, we've made significant improvements in the business.

In terms of improvement, part of our Masco operating system, we believe all our businesses can get better. So there's certainly room for improvement and the team down there is driving just that.

John Lovallo
Analyst, UBS Securities LLC

Q

Makes sense. And then if we think about PRO paint initiative at Home Depot and sort of the way we've thought about it, at least, is that there's a contractor that goes to Home Depot that historically has left without paint. Now, the idea is to sort of get that contractor to buy paint. What are the aspirations for this business as we move forward, though? Is it ultimately to move up to the larger contractor over time or is there still the focus on that sort of one or two truck contractor?

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

When you think about this business and when we really started this initiative, say, 10 years ago, we were doing tens of millions in revenue and we're doing $900 million now.

John Lovallo
Analyst, UBS Securities LLC
Q

Yeah.

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

So, we are getting at some of those other types of paint contractors that you mentioned. And our focus is really to continue to develop our relationship with the Home Depot consumer. And so, where Home Depot has their focus and where they go with their consumer, we're there to support that. And that does involve going after bigger contractors, some of the commercial contractors as well.

But fundamentally, as I said before, with our portfolio is about understanding that consumer and what they value. And we've been ticking away at that, as I said, for the better part of a decade of making our purchase decisions – or excuse me, making the purchasing process more frictionless for that [indiscernible] (00:17:48) contractor. And that is really what's driven the growth and it's been a wonderful partnership with Home Depot and that's going to continue.

John Lovallo
Analyst, UBS Securities LLC
Q

Got it. Okay. Let's talk about just – let's move on with the portfolio and maybe talk about the market and the industry. How are you guys thinking about the consumer right now? What do you see and what are your thoughts as we progress through the year here?

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

Yeah, John. It's definitely an adjustment period. They are absorbing [ph] they being (00:18:14) the consumers and absorbing significant inflation, coming to grips with a lot of noise that's out there with regards to geopolitical concerns and energy concerns, most recently with the debt ceiling and with the rate hikes and there's a lot coming at the consumer right now. So I think there's an adjustment period.

But, we're seeing a significant and have seen a significant correlation to, again, low ticket repair and remodeling is home equity. And the home equity is very strong and that's, as I mentioned, solidly correlated to repair and remodeling. So, in that regard, the consumer has strong equity. The relationship with the home has clearly changed during the COVID and that's not going back. I mean, there will be some return to work. It won't be completely. But the way consumers view their home has changed. It's the home school, it's the home office, it's the home gym, it's different and with that comes a desire to remodel your home.

John Lovallo
Analyst, UBS Securities LLC
Q

Makes sense. Maybe I'll pause for a second here just to remind everyone that if you want to ask questions and we received a few here, please do via the app and I'll be happy to incorporate them. All right. So Home Depot,

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obviously, a very strong relationship there. The big box retailers have both sort of indicated that some of the bigger ticket items, it's been a little bit more slowing than on the smaller ticket and to your earlier comment, this is where Masco plays, in the smaller ticket R&R-focused products. I mean, how do you view this sort of environment for Masco in terms of gaining share and outperforming?

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

A

Oh, it's an excellent opportunity for us. And again, it comes through two main areas. One is portfolio reconfiguration. Two, we had large ticket, new construction-oriented portfolio that we've changed now to a small ticket, repair and remodel, say 90% repair and remodel, 10% new construction, all but for our spas are low ticket.

So, again, the objective of our portfolio and we've worked hard with our operating system to reduce the variability of margin between various channels, between various geographies, between various price points and the assortment. We've endeavored to have the portfolio configured so that we're agnostic to shifts that may or may not happen from big ticket to small ticket. As I said, we're small ticket R&R company, but those small tickets are always redone when you have the big ticket.

Renovation, we've worked to reduce the margin variability by channel, be it trade or retail, and by installer, be it pro or a do-it-yourself or so. Fundamentally, what we're driving with our equity is to appeal, as I said before, to an investor who wants to get into the housing space, but wants the comfort of having that stability to be able to consistently deliver double-digit EPS through cycles, and that's the beauty of the position.

John Lovallo
Analyst, UBS Securities LLC

Q

Makes sense. Okay. How do inventories look across your channels at this point? I mean, maybe, I don't know, if you like compared to last year versus prior quarter, how are you feeling about where things sit today?

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

A

We did not experience the channel stocking and destocking phenomenon like some of other companies in our space have talked about. It's been fairly consistent. And by consistent, I mean it's normal for our channels to fluctuate their inventory levels based on the time of the year, based on seasonality, based on a number of things.

And with our operating system and our ability to have high on time and full percentage rates in terms of delivery and to do that consistently, we're able to respond relatively quickly to where the channel needs to have their inventories. As we sit back now and look seasonally adjusted where they should be in, for example, coatings for the spring selling season or where we are in our plumbing business, where the inventories look in the trade channel to support global projects, for example, they're in pretty good shape.

So, our sellout is matching to the consumer, is matching quite well to our sell into the channel. So, we don't anticipate any significant restocking tailwind or destocking headwind and we haven't reflected that in our guide for the remainder of the year.

John Lovallo
Analyst, UBS Securities LLC

Q

Okay. Makes sense. In terms of the sort of headline or overall forecast for R&R that you guys are contemplating a low-double digit declines in R&R activity. If we look at what's currently going on in the market today and, your view

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of as we move forward, I mean, do you think there's more risk to the upside to that or to the downside? Are you still pretty comfortable where you sit?

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

A

Well, we've – you and I had this conversation after Q1, John, where we had a good Q1 and we maintained our forecast and in our outlook for the year, we were at the time three months into it. And fundamentally, what we see is volatility that's out there. And I don't have a crystal ball, unfortunately. And when you're faced with that kind of volatility, and not sure what's happening and what will happen, we took a more conservative approach. And I think that's paying off and how we how we looked at that.

To answer your question directly, I would say there's more – because of that conservative nature, I think there's more upside. But again, we'll see how it plays out and we're – what it really means for us, we're at the point of impact in terms of managing the business and spend. For us, it's about continuing to invest in our growth vehicles and our growth spots.

But at the same time, watching to make sure that we are prepared should the volumes go lower, that we can flex our variable cost and drive variable cost productivity. So, you'll see us continue to invest behind our PRO paint initiative. You see us driving volume with SG&A investments as we participate more in global plumbing fares and shows and adding certain resources, continuing to fund our innovation pipeline. So, those things that are paramount to our brand development, sales and winning and the recovery, we're continuing to do.

At the same time, we have hiring freezes in certain spots across the company to make sure that we're making sure to the best that we can that we're getting short-term return on incremental SG&A investment.

John Lovallo
Analyst, UBS Securities LLC

Q

Got it. Okay. And then, let's just take that one step further. Let's say that things are somewhat better than that initial outlook. I mean, where is this going to show up the

most? I mean, [ph] is it (00:25:37) going to be in the incremental margin? I mean, how do we think about – how do we think about the upside there?

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

A

Yeah. Our – we've got a nice – I believe a good control on our cost and in the decrementals, we'll have – based on our guide this year, we'll have decrementals at or below 20%. So good solid performance in decrementals. On the flip side, on the incrementals, same sort of story, but positive – on the positive side in terms of with our variable and fixed overhead, that incremental volume will drop down to profit at about 30%. So that's a nice lift should the top line be better than we're calling.

John Lovallo
Analyst, UBS Securities LLC

Q

Okay. All right. And it seems like mix across the portfolio and some of your peers have talked about it as well, has been reasonably resilient. What is the risk of [ph] trade-down (00:26:27) if things do soften a bit here? And what do you sort of owe the strength that we've seen in the mix component to thus far?

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

A

Yeah. I – the risk to the [ph] trade-down (00:26:39), as I mentioned before, we're trying to build the portfolio of businesses that are agnostic to shifts and that can take away from stability. We want this portfolio to be as stable as possible to enable us to deliver that double-digit EPS growth I've talked about several times already.

So part of that work has been to put our production system to work to close the margin gap or reduce the margin gap from, say, lower price point products to the premium products. Now, we're not there. Same sort of thing when you talk about pro to consumer, to consumer or trade to retail, or China to Germany. So that as these shifts happen, we're reliable. And we've done that, done a pretty good job of closing that gap on the lower, lower, should there be a trade down. We would experience some margin compression if that happens. But we really haven't seen much of that.

I think at the end of the day, even when times are a little tough and people maybe are not feeling as sure in terms of financial footing as they might have prior to, what, the slowdown, we – they value the brands and, we also choose to play in China, for example, where we're in the high end and we're there by design and that is a good spot for our Hansgrohe brand.

And so, when the country shut down, the last – to see the volume reduction, we saw the [ph] volume (00:28:14) reduction was the high end and the first to see the recovery was the high end for obvious reasons. So, I think where we play coupled with our brand strength is all part and parcel of that.

John Lovallo
Analyst, UBS Securities LLC

Q

Yes. Makes sense. Okay. Let's move on to a few Plumbing-related questions here. If we think about the opportunity for incremental pricing, it seems like it's pretty appealing in the Plumbing business. Where are those pricing opportunities? Is there particular products or regions that you're seeing that?

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

A

It's more product related than region related, I would say, and that has to do with the timing of how some of the commodity increases flowed through to us and then into our P&L. So we had to do a little bit of catch-up on certain product categories more so that I would say than channel categories. Over in Europe, we also had some catch-up to do that and we've implemented, not across the whole assortment, but in parts some price increase, not relative to what we put in place last year, it's a fraction of it.

John Lovallo
Analyst, UBS Securities LLC

Q

Yeah.

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

A

But we have driven some additional pricing this year in Plumbing.

John Lovallo
Analyst, UBS Securities LLC

Q

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And how has been the reaction from your channel partners? They've been pretty receptive to that or...

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

A

It's been – in my 27 years with – in this industry, I have not seen this kind of rapid commodity escalation before and you couple that with abnormally high demand, it made for atypical pricing discussions. There was an understood need to get pricing. There was a capacity constraint. The consumers understood the inflation and were willing to pay for that. [ph] A lot of (00:30:06) very solid savings on the part of the consumer.

So, it was a different pricing environment than usual. And I would say in our targeted price increases that we've executed this year, it's been [ph] along that same ilk that (00:30:18) it's understood and pretty clear. Having said that, [ph] price is price and it's always an (00:30:25) negotiation.

John Lovallo
Analyst, UBS Securities LLC

Q

Yeah. Yeah. For sure. Okay. And we talked about Watkins and how robust things were, a bit of a pullback on a year-over-year basis in the first quarter off of very high levels. What expectation for Watkins is embedded in the full-year outlook for Plumbing?

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

A

Again off of incredible, I think it was north of 50% growth over the last two years. So, incredible growth. So, we're calling this year to be down double-digits. And if you look, interestingly enough, I talked about this a little earlier. If you look at where we're calling 2023 and you take 2019 [indiscernible] (00:31:05) pre-pandemic levels and apply a traditional growth rate to that from 2019 to 2023, even with the down double-digits, we'll be above that level. So, strong business, good fundamental tailwind with the importance of mental and physical health and well-being and how much sitting in bubbling and hot water helps with that. It's a good tailwind and a really strong business, global leader.

John Lovallo
Analyst, UBS Securities LLC

Q

Yeah. Okay. All right. Let's talk about the Decorative Architectural business. You mentioned gaining some shelf space in the quarter. Is it possible to size maybe how much space you guys took on a relative basis?

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

A

Yeah. We haven't talked specifically about that. But nice adjacency growth for us in [ph] corks (00:31:54) and sealants and into exterior stains, aerosols. And so, it's -when you aggregate it up, while we haven't talked specifically about it, it's a nice number. And importantly, when we continue – as we continue to get more adjacent products and more shelf space, it's a real billboard for the Behr brand to be able to see that out there and justifiably so the consumer has confidence in that and that helps give us leverage as we go on to other categories.

John Lovallo
Analyst, UBS Securities LLC

Q

Were those gains contemplated in the original outlook?

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

A

Yes, they were. We had a heads-up and expectations to make those.

John Lovallo
Analyst, UBS Securities LLC

Q

Got it. Okay. And thinking about PRO paint, it's about 35% of paint sales right now. Where can this go? And if you think about the margin profile between DIY and Pro, where's – how does this stand today and where do you see the opportunities?

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

A

Well, where it can go is to continue to outgrow the market. So, we've had significant share gains associated with our ability to – with the ability of the Behr team to really – from a supply chain perspective, research and development department, to really manage the supply chain challenges that we have and manage them well. And we've got the ability to get our product into the guns and rollers of new customers, but also significantly increased share of wallet of existing customers. And that – the Net Promoter Scores and the performance that we're seeing from these customers is quite impressive. And so, the – while we're facing some tough comps coming up...

John Lovallo
Analyst, UBS Securities LLC

Q

Yeah.

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

A

...the stickiness of that share gain has been impressive, and I'm really proud of the team for being able to deliver that. The DIY is a little bit better margin than PRO, but we've significantly closed that gap. So where it can go in our view, when you look at the PRO paint market, it's about, rough numbers, $10 billion and we're at $900 million. So, I think we have significant headroom to continue to grow above market.

John Lovallo
Analyst, UBS Securities LLC

Q

Makes sense. And maybe stick with DIY for a moment. I mean, when do you think those volumes kind of turn positive again? And when you think about the millennial cohort, are they more inclined to be DIYers? I mean, there's a lot of different conflicting views out there. How do you guys kind of think about it?

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

A

Well, it's obviously a big cohort stating the obvious and some changes are happening, right. While it's pretty clear that there are some difference with that – differences with that cohort in terms of, say, family formations happening later than previous generations, they're happening. And when those households form family formation, kids arrive, that cohort tends to be more owners than renters. And owners spend more money on their house than renters.

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And when we look at our research and research of a couple of firms that we follow, we're seeing that not only are these – this cohort, the millennials, willing to pick up a paintbrush and a screwdriver and, they learn differently. I learned how to do that stuff from my dad.

John Lovallo
Analyst, UBS Securities LLC

Q

Right.

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

A

This cohort learns how to do it from YouTube, which is you get yelled at a lot less when you [ph] do look at YouTube than when you try with your (00:35:34) dad. It works. And they're DIYers, and not only are they DIYers, but they repeat. It's not like we're just trying this once When surveyed and asked if you intend to do multiple projects, the answer by large is yes.

So, it's a – it's most definitely a tailwind. And we're playing in the place with relatively easy projects to paint, to put in a light fixture, to put in a new faucet. So it's definitely a tailwind for us. And we're very focused on e-commerce in general, but importantly on brand building through that channel and that's where it's happening.

John Lovallo
Analyst, UBS Securities LLC

Q

Makes sense. Right. Let's talk capital allocation. We did get one question along the lines of this that I wanted to make sure we got in. Masco launched a venture capital fund a little over two years ago. What is the strategy for this? And how big of an opportunity is there?

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

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The strategy is really, I would say, twofold. One is to keep in [ph] closer (00:36:38) touch with technology and technology that could potentially find its way into our products. And two, to look for revenue growth streams and see how – if we are involved in a particular space with an investment, we can learn to be better suppliers for that space.

So, whether it's how to manage a tech start-up that's helping to develop how to better manage projects or how to manage contractors or find contractors or anything involved in that repair and remodeling space, we're interested in it. We've made a couple of, I believe, three smallish investments, and we had no issue whatsoever with SVB and the issues associated with that bank, or a lot of those venture funds bank. And we're learning a lot and we're slowly beginning to make more and more investments.

I'm personally involved with that on a monthly basis as we look at the potential, and I think I find that extremely exciting and insightful in terms of what we can learn and where we can potentially go with both technology and revenue.

John Lovallo
Analyst, UBS Securities LLC

Q

Yeah, that's interesting. Okay. In terms of free cash flow conversion, this year, it's going to be a strong year, over 100%, at least what we're forecasting. How should we think about sort of the medium-term free cash flow conversion targets of the company?

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

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Masco has historically and continues to even more so now been a relatively low CapEx business, call it, 2%, 2.5% of revenue. We have, historically with our operating system, really solid management of working capital and inventories. So, 100% free cash flow conversion is the benchmark and that's what we're shooting for. A little bit better this year as we have some better inventory performance, but going forward, midterm, 100%.

John Lovallo
Analyst, UBS Securities LLC

Q

Got it. I think we have time for maybe one more here. Maybe just give us a refresher on some of the capital allocation priorities. How you guys think about capital deployment, how does debt paydown, share repos and all that kind of fit in there?

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

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Yeah. We haven't changed our capital allocation policies. We are focused first and foremost to invest in our existing business. That's the lowest risk, best growth avenue, best shareholder return for our investments. So, we're going to continue [ph] to do (00:39:10) that. We're going to pay a meaningful dividend with a targeted payout ratio of 30%. And then, beyond that, we see our cash flow as fungible between our targeted acquisition funnel of smaller bolt-on acquisitions for paint and Plumbing. And we're not going to force it if it doesn't fit in terms of return and our strategy. We're not going to hoard the cash and we'll sweep it off into share repurchase.

John Lovallo
Analyst, UBS Securities LLC

All right. Well, that is right up against our time limit there. So, Keith, can't tell you how much we appreciate it. Thank you.

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

Thanks, John. Great to talk to you. Bye-bye.

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