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Masco Corp. (MAS)

Raymond James Institutional Investors Conference

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CORPORATE PARTICIPANTS

Richard Westenberg
Chief Financial Officer, Treasurer & VP, Masco Corp.

OTHER PARTICIPANTS

Sam J. Darkatsh
Analyst, Raymond James & Associates, Inc.

MANAGEMENT DISCUSSION SECTION

Sam J. Darkatsh
Analyst, Raymond James & Associates, Inc.

Good morning. I'm Sam Darkatsh. On behalf of Raymond James, I would like to welcome you to the Masco Corporation presentation. With us today from Masco are Chief Financial Officer, Rick Westenberg, as well as in the back of the room, Robin Zondervan, Vice President, Investor Relations and FP&A.

Rick, I think you mentioned that your presentation is about 20, 25 minutes or so, which should leave us for a few minutes of Q&A here, but the majority of the detailed Q&A will obviously be in the breakout session following. So with that, Rick, welcome back.

Richard Westenberg
Chief Financial Officer, Treasurer & VP, Masco Corp.

...Sam, and good morning, everyone. Thanks for joining. It's great to be back here at the Raymond James conference. Really appreciate everyone joining, particularly early this morning, and good morning, good afternoon for those that are joining via webcast.

As Sam mentioned, I've got some prepared remarks that are about 20-plus minutes or so. Really, I understand that there are a number of participants in the audience that are relatively new to the Masco name. So my presentation this morning will be at a bit higher level. I'll cover some of the key points, and as Sam mentioned, we'll have a few minutes at the end for Q&A and then the breakout session afterwards.

So let's get started. So with regards to Masco, Masco is a global design, manufacture and distributor of branded home improvement and building products. We generated approximately just shy of $8 billion in revenue in 2024 and on that revenue generated just shy of $1.4 billion of adjusted operating profit, which translates into an operating profit margin of 17.5%, which is notable as it is up 70 basis points relative to 2023 operating profit margin of 16.8% and up almost 200 basis points relative to 2022. And that's on a – in the context of a relatively challenged industry backdrop, and I'll talk a little bit more about our margin expansion as I go through the presentation today. But it's one of the key hallmarks of the value proposition of Masco in terms of being able to deliver strong operating performance even in challenging cyclical markets like we are faced with today.

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In addition to the operating profit is a strong cash flow profile. So we generated over $900 million of cash flow in 2024, which represented about a 96% cash flow conversion. So really strong cash flows driven by the business, relatively modest capital intensity of the business.

I think it's also worth noting that we've got about 45 manufacturing facilities globally, 29 of which are here in the United States. In addition, we've got 21 warehouse and distribution centers here in the US.

Key to Masco's strategic capability and competitive advantage are its strong brands, product innovation and customer service. And here on the bottom of the slide, you can see a large portion of our strong brands across Plumbing and Decorative Architectural, our two segments. So I thought it'd be important to show that on the opening slide.

As I mentioned, Masco is organized into two segments, Plumbing Products and Decorative Architectural Products. There's a number of common threads between the two, and I'll get into a bit more detail in each respective segment here in a moment. The common thread is each of those segments contain strong brands. They are generally low ticket and focused on the repair and remodel or R&R segment of the industry.

So Masco overall, in terms of our sales, almost 90% of our sales are in the R&R segment of the housing industry. And why that's relevant is because there's less volatility in R&R. So as we all know, the housing cycle has its ups and downs. Masco took a number of steps a few years ago to reposition its portfolio to exit doors, windows, cabinets, product components that are more cyclical or more tied to the housing industry. And so the portfolio that remains is our more low-ticket value-add brands that while are still subject to some cyclicality, tend to have more consistency through the cycle, have more consistency in terms of operating profit and cash flows.

In addition, there's a channel dynamic that there's overlap with our channels. So we've got wholesale, retail and e-commerce. I'll talk a bit more about that in a minute, but there's a lot of cohesion between our product portfolio brands.

So diving into each of our segments in a bit more detail. First, I'll start with our Plumbing Products segment. In 2024, Plumbing Products generated just shy of $5 billion of revenue. And in Plumbing Products, there are a number of businesses, but the three that I would highlight are; one, North America Plumbing; second, International Plumbing; and third is our spa and sauna business.

So our North America Plumbing business is really anchored by our Delta Plumbing business. And that's comprised of a number of brands, but focused primarily on Peerless, Delta, its namesake, and Brizo, which is an upper premium brand.

Second is our International Plumbing business, which is anchored by our hansgrohe brand and business, based out of Germany, which sells products in over 150 countries around the world, primarily focused on Europe and China, but, again, very diversified in terms of geography. And then third is our Watkins Wellness business, which is our spa and sauna business, which has really great dynamics with regards to participating in the wellness secular trend in the market.

With regards to overall performance, as I mentioned, the segment generated approximately $5 billion of revenue. On that revenue generated 19% operating profit margins in 2024, and that was up 100 basis points from 2023, where we generated 18% operating profit margins. And that's on a relatively flattish top-line. So really great operational execution and performance despite a challenging environment.

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With regards to channel mix, Plumbing segment generates just over 50% of its revenue from wholesale, 19% from retail, 11% from specialty dealer. That is really driven based off our Watkins Wellness independent dealer network, which, by the way, majority of which are exclusive to Watkins Wellness. And then 18% e-commerce, which is heavily skewed to the Delta business.

And Delta is really well positioned from an e-commerce perspective. They're actually a leader from a decorative faucet and showerhead e-commerce business. And it's really a product of the investment and the focus that Delta has had on e-commerce. And we are over-indexed relative to the market in terms of e-commerce sales. And that's a growing area in terms of a channel distribution opportunity for Masco.

Our second segment is the Decorative Architectural Products segment. And in this segment, we generated approximately $3 billion of revenue in 2024. Decorative Architectural Products or DAP segment for Masco is comprised primarily now of two businesses, the Behr Paint, our coatings business, as well as the Liberty Hardware business, which are pulls and knobs for the kitchen bath as well as shower doors.

In our 2024 results is inclusive of business Kichler Lighting that many of you may have heard we sold and closed that transaction in Q3 of 2024. So it is partially in our results in 2024, but going forward, Kichler Lighting will be excluded from our results.

So the lion's share of this segment is really our Behr Paint and coatings business. It's about 85% to 90% of our sales in that segment. And Behr Paint is a preeminent leader in paint and coatings in North America, and has historically been very strong in the DIY or do-it-yourself portion of the business, but has continued to grow and perform strongly in the PRO portion of the business.

And we have partnered with The Home Depot. So we have an exclusive relationship with Behr Paint sold exclusively through The Home Depot channel. And it's been a great partnership that dates back over 40 years and has allowed us to be very successful together in terms of growing the paint business, both DIY and PRO. But I think it's worth noting, particularly the with the focus on PRO, the success that we have had collectively in terms of growing the PRO paint business. Through a number of initiatives, such as sales reps, delivery options such as order online, pick up in store as well as loyalty programs, we and The Home Depot have grown the PRO paint business for Masco and for Behr by over 70% since 2020 to over $900 million in 2024, a real sizable business. And we're expecting that momentum to continue. We've guided that we expect PRO paint to grow about mid-single digits here in 2025.

In terms of performance, as I mentioned, the segment generated approximately $3 billion in 2024 and 18.5% margin. So, again, very strong margins. And that is up 70 basis points on a year-over-year basis, so up versus 17.8% in 2023. The channel mix is skewed and the vast majority is to retail, again, really driven based off of the relationship with The Home Depot with Behr Paint, but also with our Liberty Hardware business as well.

As I mentioned earlier, the three key pillars for Masco and our competitive positioning are brands, product innovation and service. This slide is designed to talk about the second of that, product innovation. And what you can see on the slide are a number of products on the right hand side that speak to a number of innovations, and that is product, that is technology, that is design.

And you can see, just to cite a few, water filtration that Delta has recently introduced, both in terms of under sink as well as shower, spray paint, FreshWater IQ, which is a water management and monitoring system for your spa that checks the chemistry of your spa and digitally connects to the owner to provide readings to make sure that

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your chemistry and your spa stays where it needs to be. And then also to – Watkins Wellness has launched a cold plunge product in the business, in the channel.

So the way we track our progress and performance with regards to product innovation is through Vitality Index. And we measure vitality as the percent of our revenue in any given year that is generated by products introduced within the last three years. And our historical performance as well as our target is to have a Vitality Index of 25%. And we've continued to invest in the business and our products to deliver on a 25% Vitality Index, and we're committed to that index going forward.

It's really important, as you would imagine, to get fresh products into the market to help drive sales and growth, but it's also important to keep the freshness in the showrooms to keep the excitement of our channel partners, sales agents as well as to drive foot traffic. So it's a very important metric that we track very closely.

In terms of distribution and diversification, there are a couple of dimensions to look at this. One is from a price ladder perspective. And we go to market, generally speaking, on a good, better, best portfolio perspective. And I'll take Delta Faucet as an example of that execution.

So Delta Faucet has three plus brands. One brand, Peerless, is for the cost conscious or price sensitive consumer. And that is in place squarely in the good segment. The Delta namesake brand, which is for mainstream customers, is in the better. And Brizo, which is an upper premium, is in the best segment.

We also announced recently an internal consolidation of the Newport Brass brand into Delta. And that is another opportunity for us to leverage the growth opportunity in the best segment or the luxury segment. And that allows us to participate in different price points very effectively without stretching the brand. Each brand stays within its respective swim lane, and we're able to compete effectively at all different price points.

In terms of our global diversification, 80% of Masco sales are in North America, with 20% international. The bulk of that international sales composition is the hansgrohe brand, as I mentioned before.

In terms of channel mix, we've got about a third of our business at the wholesale trade, just under half to retail. The specialty dealer composition, as I mentioned, is really driven based off of the Watkins Wellness spa, sauna and cold plunge business. And e-commerce, again, is a growing part of the business.

And with regards to PRO and DIY, I talked a bit about this in discussions with regards to the Behr Paint business, but it's just about half and half in terms of DIY and PRO. And Pro continues to be a growing part of our business and part of the industry.

One of the attractive features of Masco and where it's positioned is where – is the industry in which it participates in. As I mentioned earlier, we repositioned the portfolio to focus more on the repair and remodel or R&R segment of the housing industry, and the R&R industry has a lot of fundamental advantages. The historical growth of the R&R industry and what we expected to realize in the medium to longer term is 1% to 2% above GDP. So think about that as 3% to 4%. And I'm referring to now really the United States market.

And a few of the fundamental drivers or advantages of the R&R industry are, number one, home price and home price appreciation, which is at record levels, which gives consumers and homeowners [ph] the confidence (00:17:10) in their home. Second is the age of the housing stock, which is now over an average of 40 years old. And importantly, approximately 1.7 million homes will enter what is often referred to as the prime remodeling age of 20 to 40 years old. And the relevance of that age bracket is that homeowners spend approximately 15% to 20%

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more with regards to R&R that – in the 20 to 40-year window. So we are coming across a significant growth in that cohort.

And then household formation, specifically the millennials in terms of homeownership, having children, et cetera. All of these really are strong fundamentals of the business that we expect will deliver the 1% to 2% above GDP growth here as we get through what has been a recently more challenging time post the pandemic. And critical to this is consumer confidence. As we get through some of the uncertainty with regards to policy, inflation, interest rate, we expect that will translate into a return to that fundamental growth.

As it pertains to Masco specifically, our target is to grow above market, so more in the 3% to 5% range organically, complemented by an M&A strategy that is focused on primarily bolt-on acquisitions. And by bolt-on acquisitions, what I'm referring to is acquisitions that are focused on our plumbing, coatings and wellness businesses that allow us to grow an incremental 1% to 3%. A good example of that is the Sauna360 transaction that was consummated in Q3 of 2023. That added approximately 1% of growth to Masco and was bolted on to our Watkins Wellness spa business to allow us to sell saunas through our spa distribution channel.

In terms of margin expansion, as I've referred to a couple of times, the margin expansion that we've realized over the last couple of years has been notable, particularly given the overall backdrop of the industry. But our margin objective for 2026 that we put out there a year ago is to grow our margins, from a total Masco perspective, to 18.5% in 2026, with 20% margins in the Plumbing segment and 19% to 20% in the Decorative Architectural Products segment.

Our guidance that we delivered for 2025 about a month ago was to generate 18% margins here in 2025. So, again, 17.5% in 2024, 18% in 2025 and 18.5% in 2026. In addition to the operating performance, I'll talk a bit in the next slide about capital allocation. But the capital deployment, we expect that our share buyback program will deliver 2-plus percent EPS growth in addition to a dividend that generates about 1% to 2% yield. And ultimately, when you talk about operating performance and the share buyback program, we would expect to deliver double digit EPS through the cycle, evidenced by the fact that we delivered 12% EPS CAGR over the last five years between 2019 and 2024.

So with regards to capital allocation, we have a very disciplined and consistent allocation framework. First and foremost, we invest in the business, and investment levels for Masco are generally in the 2% to 2.5% of sales range. For 2025, we've guided to spend about $175 million in capital, which is right in the midpoint of that range.

Second is to maintain an investment-grade credit rating. And we measure that and we manage that by maintaining a leverage ratio that is of gross debt-to-EBITDA that is below 2.5 times. At the end of 2024, we were just under that at about 1.9 times. And we've maintained a BBB or BBB equivalent credit rating. And for us, that's very important to make sure we've got stability, that we've got access to capital markets.

Third is to maintain a relevant dividend. Our target dividend payout ratio is 30%. And we, in February, announced that we were increasing our dividend for the 12th year in a row this year.

And finally, after reinvesting in the business, maintaining an investment-grade balance sheet and maintaining a relevant dividend. We return all excess cash to shareholders or deploy that towards M&A. M&A is episodic. But with regards to our share buyback program, it is very methodical, consistent and opportunistic. We've sized the available liquidity for share buybacks or M&A as about $600 million in 2025.

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So before I wrap up, maybe a couple comments with regards to the tariff environment. So when we released our guidance for 2025 in February, we released a guidance of an EPS range of $4.20 to $4.45 per share. That contemplated the first round of China tariffs of 10% and the net mitigation effect of that.

As we mentioned on the call, the team has done a tremendous job reducing our exposure to China imports, reducing it by 45% since 2018, so down from $825 million in 2018 to $450 million here in 2025. And they've done so in a very methodical, cost-effective way.

We continue to monitor the situation. Obviously, over the last 24 hours, there has been some updates and dynamics. We continue to monitor that situation. We have demonstrated the ability to navigate challenging situations that have faced our industry in the past, whether it's a pandemic, supply chain challenges, obviously, prior tariffs. And we're prepared to respond to mitigate those headwinds over time.

So, in summary, Masco participates in a very attractive R&R market that has strong fundamentals. Second, Masco is really well positioned with our brands, our products and our service to outperform the market, to grow above market and to expand margins. And third, Masco has a very disciplined, consistent and very transparent capital allocation framework that's focused on investing in the business, maintaining an investment-grade balance sheet and returning cash to shareholders to drive shareholder value.

So with that, I think we may have a few minutes for Q&A.

QUESTION AND ANSWER SECTION

Sam J. Darkatsh
Analyst, Raymond James & Associates, Inc.

Q

Thanks, Rick. Questions for Rick. Right here in the front.

Q

Yes. [indiscernible] (00:25:12-00:25:27)

Sam J. Darkatsh
Analyst, Raymond James & Associates, Inc.

Q

Repeat the question.

Richard Westenberg
Chief Financial Officer, Treasurer & VP, Masco Corp.

A

Yeah. So the question is, with regards to paint specifically, what the supply chain looks like, particularly geographically, with regards to some of the input costs. So with regards to our exposure to imports and tariffs, it's fairly limited on the Decorative Architectural Product or the paint business. There is some, but the vast majority of our exposure is really on the Plumbing segment. So right now, as we stand today, it's fairly manageable from a paint perspective.

Sam J. Darkatsh
Analyst, Raymond James & Associates, Inc.

Q

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Question here.

Q

So with the new proposed tariffs, how [indiscernible] (00:26:06) how would you expect that to impact the business in terms of the [ph] pricing pressures (00:26:11) through this year or [indiscernible] (00:26:18)?

Richard Westenberg
Chief Financial Officer, Treasurer & VP, Masco Corp.

A

Yeah. The question is with regards to the recently announced tariffs, what is the impact to the business, what is – how do we see that flowing through, et cetera? What I would say is it's pretty late-breaking. We've been monitoring the situation very closely.

With regards to China, we've been very transparent with regards to our exposure. It's about $450 million. So one can do the math with regards to the incremental tariffs there.

With regards to Canada, we've articulated that our exposure in terms of imports from Canada is not significant. Mexico, it is more significant. We have yet to quantify that. We will do that in due course. But the Mexico exposure is primarily focused with regards to our Watkins Wellness business. And that's in our – again, in our Plumbing Products segment, because we've got significant manufacturing operations in Mexico. We have operations in the US as well, but the vast majority of our Mexico import exposure is tied to our Wellness business.

And as it pertains to mitigating actions, we've continued to – through our supply chain efforts to reduce our exposure, specifically to China, but with regards to our overall import exposure overall in a very methodical way, and we've accelerated those efforts. Second is, we've worked with our suppliers in terms of price, in terms of reduced pricing. And third is price that we bring forth to our channel partners. And that's something that is well underway. Obviously, it's an uncertain dynamic moving environment, but that is something that we would expect to be part of – a critical part of the mitigation efforts.

Sam J. Darkatsh
Analyst, Raymond James & Associates, Inc.

Q

Have you announced pricing yet to the trade? I saw a couple of your competitors have already announced low single-digit pricing. Has Delta announced anything as of yet?

Richard Westenberg
Chief Financial Officer, Treasurer & VP, Masco Corp.

A

So with regards to pricing, we announced in our Plumbing segment, so Delta specifically, a low single-digit price increase at the beginning of this year. That was part of our regular price – standard pricing cadence. We have not yet announced or shared the price increase as it pertains to tariff mitigation. That is something that will be coming forth very shortly. But with the uncertain dynamic environment, we were looking to minimize the number of iterations with that. And so as we continue to get visibility and stability, expect that you'll see associated price increases where appropriate and necessary to help mitigate the tariff implications.

Sam J. Darkatsh
Analyst, Raymond James & Associates, Inc.

Q

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Talk about the tone of business, what you're seeing now? Home Depot and Lowe's comps look like they've softened a little bit in January and February, and you also had some noise around Home Depot's inventory levels of paint. So talk about what you're seeing in the field right now, if you could?

Richard Westenberg
Chief Financial Officer, Treasurer & VP, Masco Corp.

A

Sure. So we came out with our expectation guidance in terms of this year, in terms of our expectation, adjusted for the divestiture impact of Kichler that I mentioned earlier as well as adjusted for currency. So on a true organic basis, that our performance would be flat to slightly up low single digits, but we did indicate that we would expect to be slightly down in the first half of the year. And that's exactly what we're seeing. We're seeing continued softness as we saw closing out 2024, really across the segments.

And as Sam referenced, there was a load-in at the end of 2024 with regards to paint. And we're seeing a little bit of normalization in inventory coming from our key channel partner as it pertains to paint. And that's one of the factors that we included in terms of our guidance of slightly down in the first half of the year with regards to top-line.

Sam J. Darkatsh
Analyst, Raymond James & Associates, Inc.

We'll continue this in the breakout. Thank you, Rick.

Richard Westenberg
Chief Financial Officer, Treasurer & VP, Masco Corp.

Great. Thanks, everybody.

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