Strategy

<u>Leggett & Platt – Strategy Overview</u>

August 2018

Key Financial Metric

Total Shareholder Return is the key financial measure that we use to assess long-term performance. Our goal is to achieve TSR in the top third of the S&P 500 over the long term through an approach that employs four TSR sources: revenue growth, margin expansion, dividends, and share repurchases.

We monitor our TSR performance relative to the S&P 500 on a rolling three-year basis. While our performance has not met our top-third target, we continue to strongly believe our disciplined growth strategy and use of capital will support achievement of our goal over time.

Portfolio Management

We utilize a rigorous strategic planning process to help guide decisions regarding business unit roles, capital allocation priorities, and new areas in which to grow. We review the portfolio classifications of each unit on an annual basis to determine its appropriate role (Grow, Core, Fix, or Divest). This review includes criteria such as competitive position, market attractiveness, business unit size, and fit within our overall objectives, as well as financial indicators such as business unit return, growth of EBIT, EBIT margin, EBITDA, and operating cash flows. Business units in the Grow category should provide avenues for profitable growth from competitively advantaged positions in attractive markets. Core business units are expected to enhance productivity, improve market share, and generate cash flow from operations while using minimal capital. To remain in the portfolio, business units are expected to consistently generate after-tax returns in excess of our cost of capital. Business units that fail to consistently attain minimum return goals will be moved to the Fix or Divest categories.

Disciplined Growth

For quite some time we have envisioned profitable revenue growth as the main driver of our TSR. In 2016, we revised our TSR framework to moderately increase the expected long-term contribution from revenue growth to 6-9% (from 4-5% previously). Over the last three years, we have generated combined volume and acquisition growth of 5% per year on average, but this growth was partially offset by divestitures, commodity deflation, and currency impact.

We expect revenue growth to continue coming primarily from organic sources – opportunities we have developed within our Grow businesses (such as Automotive, Bedding, Adjustable Bed, Work Furniture, Geo Components, and Aerospace) along with market growth - and be augmented by carefully screened, strategic acquisitions that meet our established criteria.

Recent Growth Sources should continue for at least the next few years. The combination of content gain, market growth, and small bolt-on acquisitions should enable us to achieve our growth target for the foreseeable future. To ensure continuing success, we have implemented a **Growth Identification Process** to generate additional growth opportunities in our <u>current markets</u>. By better understanding our competitive strengths, customer needs, and market trends, we have widened our lens to seek further growth in current markets. In addition, we are utilizing our **Styles of Competition** to identify longer-term opportunities in <u>new, faster-growing markets</u> where we do not currently participate, but where we would have a sustainable competitive advantage.

As mentioned above, our long-term growth objective envisions periodic acquisitions. We primarily seek acquisitions within our Grow businesses, and look for opportunities to enter new, higher growth markets (carefully screened for sustainable competitive advantage). We expect all acquisitions to (a) have a clear strategic rationale, a sustainable competitive advantage, a strong fit with the company, and be in an attractive and growing market; (b) create value by enhancing TSR; (c) for stand-alone businesses: generally possess annual revenue in excess of $50 million, strong management, and future growth opportunity with a strong market position in a market growing faster than GDP; and (d) for bolt-on businesses: generally possess revenue in excess of $15 million, significant synergies, and a strategic fit with an existing business unit.

Returning Cash to Shareholders

Leggett & Platt has consistently been a strong cash generator. During the past three years, we produced $1.4 billion of operating cash, and we returned much of this cash to shareholders in the form of dividends and share repurchases.

Our target for dividend payout is 50-60% of earnings, and future dividend growth should approximate earnings growth. We have increased our annual dividend for 47 consecutive years, and we plan to extend that record.

Our priorities for use of cash are: 1) fund organic growth in attractive businesses, 2) pay dividends, 3) fund strategic acquisitions, and 4) repurchase stock with available cash, if any remains. We have a standing authorization from the Board to buy up to 10 million shares each year; however, no specific repurchase commitment or timetable has been established. We assume an annual 1% net reduction in share count on average, which will generate 1% TSR annually. However, it is likely that there will be some years with little or no share reduction (i.e. when growth and acquisitions have used most or all of the available capital).

Management Compensation

Our incentive programs reward strong performance. Senior executives participate in an incentive program with a three-year performance period equally weighted on (1) relative TSR compared to the performance of a group of approximately 320 peers; and (2) company or segment EBIT CAGR. Annual bonuses at the business unit level emphasize the achievement of higher return on assets along with free cash flow generation.

TSR in Top Third of S&P 500

Sources of TSR: Growth, Margin Improvement, Dividend Yield, and Share Buybacks

Total Shareholder Return = (Δ Stock Price + Dividends) / Initial Price

Revenue Growth Target:	6-9% annually
Margin Improvement:	Growth in attractive markets, product development, cost savings, efficiency impr.
Dividend Payout Target:	50-60% of earnings
Excess Cash Use:	Stock Buyback

Growth Framework

- Targeting 6-9% average annual revenue growth; organic + acquisition
- Three avenues of growth:
  1. **Recent Growth Sources** should continue for at least next few years
  2. Implemented a **Growth Identification Process** → to generate profitable growth initiatives in current markets
  3. Utilizing our **Styles of Competition** → to identify longer-term opportunities in new attractive markets

Enhanced framework for consistent, disciplined long-term profitable growth

1. Recent Growth Sources

- Market growth + **Other Sources**
  - Targeting 8% annual growth through 2020
- **Other Sources** include:
  - Content gains in Automotive and Bedding
  - Adjustable Bed share gains and market growth
- Program awards, customer focus, consumer preference trends support growth for at least the next few years
- Acquisitions should also contribute to growth
  - Averaged ~2% acquisition growth over past several years

2. Growth Identification Process

- Implemented **Growth Toolkit** to generate profitable growth initiatives in current markets
- Toolkit framework:
  1. Analyze our current markets and define attractive spaces for growth
  2. Identify specific opportunities within spaces of interest and prioritize based on potential for value creation
  3. Determine action plans, including both **Organic** and **Acquisition** initiatives

3. Styles of Competition

- Defines and measures **"fit"** based on fundamentals of where and how we currently compete
- Lens used longer term to identify, screen, and pursue opportunities across **more diverse spaces and faster-growing markets**
- Leggett's predominant style is **Critical Components**
  - ~60% of sales; typically higher margins/returns
  - Majority of recent sales growth
- Precision Hydraulic Cylinders acquired January 31, 2018

PHC Acquisition

- PHC annual revenue of ~$85 million; slightly EPS accretive
- Formed new growth platform in Hydraulic Cylinders
- $5 billion addressable market; primarily construction equipment, material handling, and transportation
  - Global market growth ~5%+
  - Growth via: geographic expansion + penetration in existing markets
- Strong fit with "Critical Components" Style of Competition
  - Highly engineered, co-designed components
  - Long product life cycles
  - Small part of end product's total cost
  - Many large OEM customers

Critical Components Style Defined

		Dimension	Characteristic
Where we compete	Product / Service / Solution	1. Role in value chain	**Translate RM or components** into critical component
		2. Functional role	**Functionally essential** to end product
		3. % of finished COGS	**<25%** of finished COGS
	Industry Structure	4. Customer set	Concentrated in **few large customers**
		5. Competitive set	**Small private** companies w/ single focus
	Econ-omics	6. Gross margin	Earns **attractive returns** at ~20-30% GM
		7. Asset intensity	**Light manufacturing** ~2x asset turns
How we compete		8. Deep customer engagements	**Deep understanding of customer** design, production pain points, long-term relationships
		9. Collaborative design	**Co-design** products/components for **better functionality** and lower total cost
		10. Flexible mfg	**Long-run SKUs** that can be adjusted to deliver **custom specs** w/ minimal additional capital
		11. Continuous cost improvement	**Continuous cost improvement** throughout life of long run-length SKUs

Acquisition Criteria Unchanged

- Strategy: clear strategic rationale; sustainable competitive advantage; strong **"fit"** with L&P
- Financials: TSR accretive; IRR > 10%
- **New Platforms**: revenue > $50m; strong management; subsequent growth opportunity
  - Mkt size > $250m; growing > GDP
  - Industry EBIT margin approximates Leggett's average
- **Add-on** businesses: revenue > $15m; significant synergy; strategic fit in an existing BU

Sources of Margin Improvement

Short-Term Opportunities:

- Recover Cost Inflation
  - 2017/1H 2018 margins impacted by RM pricing lag
  - Typically catch up w/ pricing when costs stabilize
- Expanding **metal margin**
  - Steel rod prices increase while scrap costs stabilize

Longer Term Opportunities:

- **Portfolio management**
  - Continue to invest in our advantaged businesses
  - Improve or exit low-margin operations
- **New products** with higher margins
- Incremental **volume**
  - **25-35%** contribution margin <u>in businesses with spare capacity</u>
- **Continuous improvement**
  - Management tools
  - Cost reduction, efficiency, etc.

Priorities for Use of Cash

1. Fund organic growth in attractive businesses
   - Capital expenditures
   - Working capital investments
2. Increase dividends
   - **47 year history** of dividend increases
     - Member of S&P *Dividend Aristocrats*
3. Fund strategic acquisitions
4. Repurchase stock with available cash, if any remains

Operating Cash has exceeded Dividends &
Capital Expenditures every year for nearly 30 years

OTHER STRATEGY DETAILS

Leggett & Platt®

Strategic Shift Outlined in 2007

What We Said:

Goal = TSR in top third of S&P 500

Sources: Growth, Margin Improvement, Dividend Yield, and Share Buybacks

3 STEPS:

1. **FOCUS** by divesting low performing businesses
2. **IMPROVE** margins & returns on assets we keep
3. **GROW** revenue, long-term, at 4-5% annually

- Successfully executed **"Focus"** and **"Improve"**
- Now turning more attention to **Growth**

Role-Based Portfolio Management

- Strategic Planning Process
  - Assess market attractiveness and Leggett's advantages
  - 3-year plan to achieve ≥ 10% TBR/year
  - Used to determine portfolio role
- Place each BU into Portfolio Role
  - Grow, core, fix, or divest
  - Different goals for each
    - Grow: profitable **Growth**
    - Core: maximize **Cash**
    - Fix: rapidly **Improve**

Criteria for Role Assignments

	GROW	CORE	FIX / DIVEST
1. COMPETITIVE POSITION	Advantaged	Solid, Stable	Tenuous or Disadvantaged
2. MARKET ATTRACTIVE?	Strong, Growing	Attractive, but with Lower Growth Potential	Poor or Declining
3. FIT w/ LEGGETT	Strong	Strong	Limited
4. RETURN (ROGI)	Consistently > 12%	Stable, 9-12%	Erratic or < WACC
5. BU SIZE & MATERIALITY	Large, Significant	Large, Significant	Inconsequential, Distracting

Expectations by Portfolio Role

- All: Credible Path to ≥ 10% TBR Required, else Exit

- Grow: Provide Profitable **Growth**; Return > WACC
  - Invest capital in competitively advantaged positions
  - Identify major organic, M&A, or rollup investments

- Core: **Generate Cash**; Return ≥ WACC
  - Maintain stable, competitive positions to generate cash
  - Aggressively improve EBITDA and free cash flow
  - Profitably grow market share, but with minimal capex
  - Enhance productivity; reduce costs, overhead, working capital

- Fix: **Rapidly** Restructure, else Exit
  - Limited time to achieve return ≥ WACC, else divest / liquidate

Financial Metrics Defined

- TSR: Total Shareholder Return
  - Total benefit investor realizes from owning our stock
  - (Δ stock price + dividends) / initial stock price
- EBIT CAGR: Compound Annual Growth Rate of EBIT
- ROCE: Return on Capital Employed
  - Drives ~60-70% of annual bonus at operating level and corporate
  - EBIT / (working capital (ex cash & current debt) + net PP&E)
- FCF: Free Cash Flow
  - Drives ~20-30% of annual bonus at operating level and corporate
  - EBITDA – capex +/– Δ working capital (ex cash & current debt)

TSR PERFORMANCE

	Prior Targets	07-10	08-11	09-12	10-13	11-14	12-15	13-16	14-17	15-18[2]	17-20e[4]	Current Targets
		3-Year CAGRs										
Revenue Change	**4-5**	(7)	(4)	7	4	5	5	3	2	3	8	**6-9**
ex divest/deflat./currency						*5*	*7*	*7*	*5*	*5*		
Margin Change	**2-3**	(1)	4	4	3	6	11	12	6	4	3	**1**
Change in Multiple	**--**	12	11	(4)	2	12	(2)	--	(5)	(3)	1	**--**
Dividend Yield	**3-4**	6	5	5	5	4	4	3	3	3	3	**3**
Stock Buyback	**2-4**	6	4	2	2	1	2	2	1	1	1	**1**
Annual TSR	**12-15**	**16**	**20**	**14**	**16**	**28**	**20**	**20**	**7**	**8**	**16**	**11-14**
% Rank in S&P 500[1]		***8%***	***38%***	***36%***	***48%***	***25%***	***31%***	***11%***	***56%***	***75%[3]***		

[1]1% is best.

[2]TSR estimate based on mid-point of 2018 guidance and assumes a $48 year-end share price.

[3]Relative TSR performance through July 2018.

[4]TSR estimate based on 2020 operating targets.