03-May-2022

Leggett & Platt, Inc. (LEG)

Q1 2022 Earnings Call

CORPORATE PARTICIPANTS

Susan R. McCoy
Senior Vice President-Investor Relations, Leggett & Platt, Inc.

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

Jeffrey L. Tate
Executive Vice President & Chief Financial Officer, Leggett & Platt, Inc.

Tyson Hagale
Senior Vice President, President-Bedding Products, Leggett & Platt, Inc.

Steven K. Henderson
Executive Vice President, President-Specialized Products and Furniture, Flooring & Textile Products, Leggett & Platt, Inc.

OTHER PARTICIPANTS

Susan Maklari
Analyst, Goldman Sachs & Co. LLC

Keith Hughes
Analyst, Truist Securities, Inc.

Bobby Griffin
Analyst, Raymond James & Associates, Inc.

Peter Jacob Keith
Analyst, Piper Sandler & Co.

MANAGEMENT DISCUSSION SECTION

Operator: Greetings and welcome to Leggett & Platt First Quarter 2022 Earnings Conference Call. At this time, all participants are in listen-only mode. A brief question-and-answer session will follow the formal presentation. [Operator Instructions] As a reminder, this conference is being recorded.

And now it is now my pleasure to introduce your host, Susan McCoy, Senior Vice President of Investor Relations. Thank you and over to you, ma'am.

Susan R. McCoy
Senior Vice President-Investor Relations, Leggett & Platt, Inc.

Good morning and thank you for taking part in Leggett & Platt's first quarter conference call. On the call today are Mitch Dolloff, President and CEO; Jeff Tate, Executive Vice President and CFO; Steve Henderson, Executive Vice President and President of the Specialized Products and Furniture, Flooring & Textile Products segments; Tyson Hagale, Senior Vice President and President of the Bedding Products segment; and Cassie Branscum, Senior Director of IR.

The agenda for our call this morning is as follows: Mitch will start with a summary of the main points we made in yesterday's press release and discuss operating results and demand trends, Jeff will cover financial details and address our outlook for 2022, and Mitch will conclude the call with some comments on our recently issued Sustainability Report.

This conference call is being recorded for Leggett & Platt in its copyrighted material. This call may not be transcribed, recorded, or broadcast without our express permission. A replay is available from the IR portion of Leggett's website. We posted to the IR portion of the website yesterday's press release and a set of PowerPoint slides that contain summary financial information along with segment details. Those documents supplement the information we discuss on this call, including non-GAAP reconciliations.

I need to remind you that remarks today concerning future expectations, events, objectives, strategies, trends, or results constitute forward-looking statements. Actual results or events may differ materially due to a number of risks and uncertainties and the company undertakes no obligation to update or revise these statements. For a summary of these risk factors and additional information, please refer to yesterday's press release and the sections in our most recent 10-K entitled Risk Factors and Forward-Looking Statements.

I'll now turn the call over to Mitch.

J. Mitchell Dolloff

President, Chief Executive Officer & Director, Leggett & Platt, Inc.

Good morning. Thank you all for participating in our first quarter call. Yesterday, we reported first quarter results, largely in line with our expectations. Sales from continuing operations were $1.32 billion, EBIT was $138 million and earnings per share was $0.66. Sales in the quarter were up 15% versus first quarter 2021, reflecting our successful pass-through of significant inflation over the past several quarters, partially offset by lower volume.

EBIT increased 8%, primarily from expanded metal margins in our Steel Rod business and pricing discipline in our Furniture, Flooring, & Textiles segment, partially offset by lower volume and higher raw material and transportation costs in Automotive generally and production inefficiencies and related premium freight costs in a North American automotive facility. EPS of $0.66 was a 3% increase versus $0.64 in first quarter of 2021.

Our full-year guidance remains unchanged as we balance strong first quarter results with continuing macro market uncertainties, including supply chain constraints, inflation, tighter monetary policy, the invasion of Ukraine, and COVID lockdowns in China. While our direct business exposure to Ukraine and Russia is minor, our thoughts, concern, and hope go out to those impacted by the ongoing conflict.

Moving on to the segments, sales in our Bedding Products segment were up 19% versus first quarter of 2021, primarily from raw material-related selling price increases and the Kayfoam acquisition in Europe. Volume was down primarily due to softness as expected in US and European market demand. Market demand remained soft in the first quarter due to reduced consumer activity and elevated inventory levels across the industry. Raw material, transportation, and labor costs continue to increase and we are carefully managing the impact and passing along cost as necessary.

Supply chain constraints have generally improved across the Bedding businesses. We are making progress in reducing certain inventories built under higher demand expectations, but we will make sure that we can still comfortably support near-term customer requirements and protect against future disruptions.

We also successfully completed the reheat furnace replacement at our steel rod mill, enabling us to begin reducing the extra rod inventory we built for safety stock. We expect demand softness to continue throughout the second quarter. Provided no major changes in the macroeconomic backdrop, we would expect gradual sequential improvement throughout the second half of the year. This should result in full-year mattress-related volume down mid-single digits. We expect full-year volume for the segment overall to be flat to down mid-single digits, reflecting greater strength in other parts of the business.

EBITDA margins in the segment were lower versus first quarter 2021, primarily from lower volume; lower overhead absorption as production and inventory levels were adjusted to meet reduced demand; and continued investment in labor, given difficulties in hiring and training, mostly offset by expanded metal margin in our Steel Rod business.

Sales in our Specialized Products segment increased 2% versus first quarter 2021 from growth in Aerospace and Hydraulics Cylinders. Automotive volume was down slightly. The industry forecast for global automotive production has come down since the beginning of the year, primarily as a result of Russia's invasion of Ukraine and the ongoing conflict. The most significant reductions are in Europe, but all geographies are impacted to varying degrees. We anticipated reductions to industry forecast in our initial guidance, so these changes are less impactful to our outlook.

Consumer demand remains strong and vehicle inventory remains at record low levels. As supply chains begin to stabilize, the industry should see improving production in the second half of 2022. Industry forecasts now indicate recovery continuing through 2024. In our Aerospace business, demand for fabricated duct assemblies remains at pre-pandemic levels and we continue to see modest demand recovery for welded and seamless tube products. We expect continued recovery in 2022 and the industry is anticipated to return to 2019 demand levels in 2024.

End market demand in Hydraulic Cylinders is strong and order backlogs in the industry are at record levels.

However, global supply chain constraints of labor availability have hampered the ability of our OEM customers to ramp up production. It could be late 2022 or longer before industry backlogs normalize. We expect our sales in this business to continue to grow as OEM production increases.

EBITDA margins in the segment declined primarily from higher raw material and transportation costs in Automotive generally and production inefficiencies and related premium freight costs in our North American automotive facility. Sales in our Furniture, Flooring & Textiles Products segment were up 17% versus first quarter of 2021, primarily from raw material and related selling price increases and volume recovery in work furniture, partially offset by lower volume in flooring products, textiles, and home furniture. In home furniture, market demand remains – the market demand at mid-level and upper price points remains relatively strong. However, demand at lower price points has softened. This is impacting our business in China. The Chinese market also has been impacted by COVID-related lockdowns.

Work furniture sales have recovered to above pre-pandemic levels from strong demand for products sold for residential use and improvement in contract markets as companies redesign their footprints and invest in office space to attract and retain employees as more people return to the office. We expect continued growth in this business in 2022.

We expect Geo Components to grow in 2022 as demand remains strong across both civil construction and retail markets. In flooring products, residential demand has suffered with lower home improvement activity, while hospitality demand is improving but remains well below pre-pandemic levels. EBITDA margins in the segment improved versus the first quarter of 2021, primarily from pricing discipline.

Before I turn the call over to Jeff, I would like to thank our employees for your ingenuity, collaboration, and dedication. It's because of your collective efforts that we were able to once again navigate dynamic and challenging circumstances and deliver record first quarter results.

Jeffrey L. Tate

Executive Vice President & Chief Financial Officer, Leggett & Platt, Inc.

Thank you, Mitch, and good morning, everyone. In first quarter, we generated cash from operations of $39 million, up $50 million versus an $11 million use of cash in 2021. First quarter is normally our lowest cash flow quarter of the year with increased working capital, driven by the normal cadence of our business. Working capital increased significantly last year due to restocking efforts following inventory depletion in 2020, but increased to a lesser extent this year as we began to return to more normal levels of inventory.

We continue to expect cash from operations of approximately $600 million in 2022 as last year's significant inflationary impacts are not anticipated to recur and we continue to balance inventory levels. We ended the first quarter with adjusted working capital as a percentage of annualized sales of 15.2%. Our priorities for use of cash are unchanged. They include in order of priority, funding organic growth, paying dividends, funding strategic acquisitions, and share repurchases with available cash.

Total capital expenditures in the first quarter were $19 million. In February, our board of directors declared a $0.42 first quarter dividend, $0.02 or 5% higher than last year's first quarter dividend at an annual indicated dividend of $1.68, the yield is 4.7% based upon Friday's closing price of $35.63, one of the highest among the Dividend Kings.

During the quarter, we divested a small South Africa spring operation, formerly a part of International Bedding, with annual sales of approximately $8 million. With the deleveraging we accomplished over the past few years, share repurchases have returned as one of our priorities for use of cash. The level of repurchases will vary depending on various considerations, including alternative uses of cash and opportunities to repurchase shares at an attractive price.

We took advantage of the decline in share price in recent months and repurchased approximately 400,000 shares in March at an average price of $36.68 per share. Total repurchases for the quarter, including approximately 200,000 shares related to employee benefit plans, were $22 million. We ended the first quarter with net debt-to-trailing 12-month adjusted EBITDA of 2.32 times. Our strong financial base gives us flexibility when making capital and investment decisions. We remain focused on cash generation while maintaining our balance sheet strength and deploying capital in a balanced and disciplined manner that positions us to capture near- and long-term growth opportunities, both organically and through strategic acquisitions.

Now, moving to guidance. As Mitch stated earlier, our 2022 guidance is unchanged. 2022 sales are expected to be $5.3 billion to $5.6 billion or up 4% to 10% over 2021. Guidance reflects roughly flat volume overall with the Bedding Products segment flat to down mid-single digits, Specialized Products up mid to high single digits, and Furniture, Flooring, & Textile Products roughly flat. Guidance also reflects continued inflationary impact, primarily from the raw material-related price increases, including those implemented as we moved through 2021.

Acquisitions in 2021 should add 1% to sales growth, but will be partially offset by smaller divestitures. We expect volume growth in Automotive as the industry supply chain issues improve, as well as sequential improvement in production efficiencies and premium freight costs. We also expect continued recovery in Work Furniture, Aerospace, and Hydraulic Cylinders.

In Bedding, we anticipate improved operating efficiency as industry demand becomes more stable. 2022 earnings per share are expected to be in the range of $2.70 to $3. The midpoint reflects metal margin expansion in our Steel Rod business and higher volume in Automotive, partially offset by increased transportation and labor costs and reduced overhead absorption as we continue to balance inventory levels. Based upon this guidance framework, our 2022 full-year adjusted EBIT margin range should be 10.5% to 11%.

Earnings per share guidance assumes a full-year effective tax rate of 23%, depreciation and amortization to approximate $200 million, net interest expense of approximately $80 million, and fully diluted shares of 137 million. For the full year 2022, we expect capital expenditures of approximately $150 million, dividends should approximate $230 million, and share repurchases to offset share issuances.

In closing, Leggett remains well positioned both competitively and financially to capitalize on long-term opportunities in our various end markets. Our enduring fundamentals give us confidence in our ability to continue creating long-term value for our shareholders.

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

J. Mitchell Dolloff

President, Chief Executive Officer & Director, Leggett & Platt, Inc.

Thanks, Jeff. In mid-April, we issued our second Sustainability Report. We're committed to enhancing lives through our people, our products and our processes by finding new ways to care for the health and wellness of our employees and their families, attract and retain talent, develop our employees to their fullest potential, and advance our inclusion, diversity, and equity efforts, by striving to advance innovative, sustainable solutions for our customers and the end consumer, by continuing to aggressively pursue resource efficiency and conservation practices, and by ensuring a culture of good governance and high ethical standards within our businesses.

In 2022, our key ESG initiatives include conducting a materiality assessment to further define the ESG opportunities that provide the greatest value to our stakeholders and are the most meaningful to our company. Measuring and reporting our greenhouse gas emissions data, advancing our inclusion, diversity and equity efforts, evaluating opportunities for establishing key management systems to improve data collection and contribute to broader companywide sustainability advancement, and enhancing our supplier assessment process, including a heightened emphasis on labor and social standards and cybersecurity controls. We are pleased with the progress we made in 2021 and look forward to sharing the progress we make in 2022 as we continue to build and improve upon our ESG practices and processes.

With those comments, I'll turn the call over to Susan.

Susan R. McCoy

Senior Vice President-Investor Relations, Leggett & Platt, Inc.

That concludes our prepared remarks. We thank you for your attention and we'll be glad to answer your questions. Mitch will direct our Q&A session and the group will answer your questions. Bikram, we're ready to begin the Q&A.

QUESTION AND ANSWER SECTION

Operator: Thank you. Ladies and gentlemen, we will now begin the question-and-answer session. [Operator Instructions] We have our first question from the line of Susan Maklari with Goldman Sachs. Please go ahead.

Susan Maklari
Analyst, Goldman Sachs & Co. LLC

Q

Thank you. Good morning, everyone, and congrats on a good quarter. My first question is focusing on Bedding. You've obviously – see volumes down 13% this quarter in spring, in US spring, and 20% in the specialty foams business. Appreciating the commentary that you gave on the call, Mitch. But can you talk a little bit more about the demand and how the inventories within the channel are moving through and just how you're thinking about the upcoming quarters and production rates there?

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

A

Yeah. Good morning, Susan, thanks. It's a great question and something we've been talking a lot about on our side. I think it's interesting to look sort of what happened in – over the time period of last year and what we expect to happen in the first and second half of this year. But Tyson, I'll turn that over to you for the detail.

Tyson Hagale
Senior Vice President, President-Bedding Products, Leggett & Platt, Inc.

A

Sure. Good morning, Susan. You'll recall when we talked about the results in the fourth quarter that we shared our thoughts about a coming slowdown in the bedding market. And at the time, it was our thought that our position in the value chain with inventories that had been built up that we were feeling the impacts first and largely because of continued inflation and also the breakout of Omicron and we expected the start of the year to be slower and then to improve as we move through the year.

And we started off the first quarter pretty much in line with expectations. Things were slow, but at a really consistent and stable level. But once we saw the invasion of Ukraine in late February, early March, we did see some further slowdown. It was our thought that the additional shock of energy costs and also just general consumer sentiment led to some lower demand levels. But our expectation is once that shock kind of moves through the system, that we will return to some more reasonable levels of demand as we move through the year and probably getting closer to what we've seen more in historical seasonality, that we kind of add all that up and we feel like, as we go through the year, probably ending up down for the total market somewhere in the mid-single-digit range.

Susan Maklari
Analyst, Goldman Sachs & Co. LLC

Q

Okay. That's very helpful. Thank you. And I guess staying in that segment, the margin there was really impressive despite all these headwinds and moving parts that you faced in the quarter was basically flat year-over-year. Can you talk a little bit about what drove those margins? And I guess with that, too, I know you mentioned in your comments that you completed the reheat furnace replacement. And so, I think that it's especially impressive when you think about that thrown in there as well. And so, just any commentary on those margin drivers and where we are. It sounds like the reheat furnace is done and behind you, but any color there as well.

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

A

Yeah, sure. Tyson, I'll turn this over to you. But I think that, first off, it shows the diversity – the benefits of the diversity of our business overall. But even within bedding, right, that we were able to be helped by the strong spread at the rod mill. And I just want to say thanks to the team that did the work to do – complete the reheat furnace replacement. They did a great job there really anticipating any problems that might occur and were very thoughtful and careful about that. And it's great to have that back up and running. But Tyson, I'll let you add on.

Tyson Hagale
Senior Vice President, President-Bedding Products, Leggett & Platt, Inc.

A

Yeah. I think that's exactly right, Mitch. The diversity of our business, even within bedding, really does help. And we've been able to maintain overall EBIT margin year-over-year. A big part of that is the metal margin. And I think it's worth pointing out that just strong overall demand in the steel market has allowed us to sell some of our excess capacity or production into the market outside of the bedding market.

At the same time, that's helping us offset some weakness in demand in our innerspring and mattress business. But also because we saw some signs of demand slowing in the fourth quarter, we started taking some actions then to slow our production rates. And although we had, what I would call, a reasonable amount of cushion in our inventory, we did want to go ahead and start bringing that down to some more manageable levels as we got through the first part of this year. So, that also did impact our overhead recovery as well. And so you can add all that up and that's how we've kind of been able to manage keeping margins in that same kind of range.

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

A

Yeah. Tyson, maybe one more thing. Do you think that also as we've gone through the surge and the declines and we're a little bit more stable, that we've been able to improve our production efficiency?

Tyson Hagale
Senior Vice President, President-Bedding Products, Leggett & Platt, Inc.

A

Yeah. It's a good point, Mitch. I mean, also, as we've seen the slowdown in demand, it has given us an opportunity to, really across all of our business groups to get a handle on both labor, retrain employees. We've added some capacity and get to a place where we are producing more efficiently.

Susan Maklari
Analyst, Goldman Sachs & Co. LLC

Q

Okay. That's great. And then, I'm going to squeeze one more in here because it didn't get past me that you did do some share buybacks this quarter, finally, above just what was issued as part of your employee plans. And so, I guess, can you talk a little bit about the decision to get into the market here? And with that, any thoughts on how you're thinking about capital structure, targeted debt levels as you've obviously worked really hard to get that deleveraging through in the last couple of years and now sit in a much better position overall?

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

A

Yes. Thanks, Susan. And Jeff, I'll let you take that one. But I have to say it's great to be in a position to having done such great work on the deleveraging, to be able to restart the share buybacks. But Jeff, I'll let you chime in with more detail.

Jeffrey L. Tate
Executive Vice President & Chief Financial Officer, Leggett & Platt, Inc.

A

Great. Thanks, Mitch, and good morning, Susan. Appreciate the question. Yeah. From our perspective, as you mentioned, the deleveraging efforts over the past couple of years have really positioned us well in terms of having better financial flexibility, to execute on our capital allocation priorities, which you are very familiar with in terms of funding our organic growth, continue to being committed to our dividend growth, and then looking at strategic acquisitions.

Now that we're in a better leveraging space and looking at that target leverage range that we've been working on here, we felt like going through the first quarter, there were some opportunities to take advantage of the decline in our share price that we saw in recent months, which allowed us to get into the market and buy those shares that you mentioned. We're going to continue to execute on our capital allocation priorities as we go through the year while heavily focusing on our cash flow generation. And we've guided to a $600 million range at this point.

And as we continue to assess that and evaluate that versus our other alternative uses of cash, if it makes sense from a value creation perspective to go out and purchase additional shares beyond our issuances, then we'll look at that. But at this point, we're still guiding to share repurchases – basically being neutral to share issuances for the year.

Susan Maklari
Analyst, Goldman Sachs & Co. LLC

Q

Okay. Thank you for that. I'll turn it over here and good luck with everything.

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

A

Thank you, Susan.

Operator: Thank you. Your next question from the line of Keith Hughes with Truist. Please go ahead.

[Technical Difficulty] (00:25:41)

Operator: Your line is muted.

Keith Hughes
Analyst, Truist Securities, Inc.

Q

If you could just talk about...

Operator: I'm sorry. Could you please repeat the question again Keith? Thank you.

Keith Hughes
Analyst, Truist Securities, Inc.

Q

Yes. The question is on metal margins. I know it was a big help in the quarter. I just want to talk about your expectations on that here in the near term. [indiscernible] (00:25:57) prices in steel lightening up here in the last week or two? Is that a trend you expect to continue or will it have an impact?

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.
A

Yeah. Good morning, Keith, and thanks for the question. Tyson, do you want to take that one? I think we've been [indiscernible] (00:26:15) long term what's going to happen there, but I think that what we've been seeing is pretty helpful.

Tyson Hagale
Senior Vice President, President-Bedding Products, Leggett & Platt, Inc.
A

Yeah. Good morning, Keith, and Mitch is right. As we started the year, we expected metal margins overall to start tapering sometime in the second quarter. But it's been a pretty dynamic market. I mentioned that there has been relatively strong demand across steel products outside of bedding of late. And part of that is demand-driven and I think also continued inflation and conversion cost has also driven some of the pricing in rod and wire. And then on top of that, this was also another factor coming from the Ukrainian invasion, with a run-up in scrap cost. So, that's also driven more run-up in overall metal margin and rod pricing. And so, as we kind of added up all those things as we moved through the first quarter, we initially thought that that margin would start tapering in the second quarter. We think that's likely going to take some time for all that to unwind. And so more likely, it's going to stay kind of where it is or at least at an extended period back into the later part of the third quarter and into the fourth quarter. So, at least as we can see things now, like I said, it's pretty dynamic. But that's how we feel about the expectations.

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.
A

And so we said this I think at the first quarter or at the fourth quarter call, but that we still expected the spread overall on average for the year to be up over last year, we'd still say that's the case.

Tyson Hagale
Senior Vice President, President-Bedding Products, Leggett & Platt, Inc.
A

Yeah. That's right.

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.
A

And those impacts too on the – impacts broader steel market of the invasion of Ukraine impacts not only our rod business, but also flat steel, right, that applies into different parts of our business.

Keith Hughes
Analyst, Truist Securities, Inc.
Q

Okay. Thank you. And then final question. Still got a pretty wide guidance range here. What would be the top one or two variables that would swing you to the high end or swing you to the low end?

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.
A

Boy, that's so [indiscernible] (00:28:09). I'll throw it to...

Keith Hughes
Analyst, Truist Securities, Inc.
Q

Which one do you think is the most – the one that could change the...

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

A

Well, I mean, I think the question is really, what happens to the consumer demand, right? It's been – despite all of these challenges, has been holding up pretty well. So I think that's one that's out there. And do – does tightening monetary policy hit the right line and be able to help sort of level off and taper inflation without destroying that consumer demand? But I think that's probably the biggest one out there. I mean, there's certainly the Ukraine invasion, the COVID lockdown in China, all those things are potentially – are disruptive and impactful. But I think over the last couple years, we've found a way to service the consumer, not always neatly, but, you know, be able to do it despite those sorts of challenges. So we'll see.

I don't know. Jeff, Susan, is there any others that you would add in there or that you would place higher?

Jeffrey L. Tate
Executive Vice President & Chief Financial Officer, Leggett & Platt, Inc.

A

No, Mitch. I think those are some of the key drivers that we would see that could really swing the range. As we look at our guidance for the remainder of the year, I think if we were to make it more specific to our business unit based on that consumer sentiment, it would be some of the things, I think, we called out in our prepared remarks around what happens with volumes in Automotive as we go through the remainder of the year and then looking at the metal margins, which we just finished talking about.

Keith Hughes
Analyst, Truist Securities, Inc.

Q

Okay. Great. Thank you.

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

A

Yeah. Thank you, Keith.

Operator: Thank you. We have next question from the line of Bobby Griffin with Raymond James. Please go ahead.

Bobby Griffin
Analyst, Raymond James & Associates, Inc.

Q

Good morning, everybody. Thanks for taking the questions. I guess, Mitch, first, I want to look at Specialized. Obviously, a lot going on there between supply chain, higher shipping, raw materials. But trailing 12-month margin in that business on EBIT is probably around 10%. Pre-COVID was around 16%. So, can we just maybe unpack a little bit the size of the headwinds you're facing and then kind of talk about if we get back to "normal," do you – can you recapture that loss, 600 basis points of margin or are some of it probably going to be more structural now where the margin profile of that segment could be a little different going forward? Just any further detail around that.

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

A

Yeah. Good morning, Bobby. That's a great question. I'm glad that you asked it. I'll take a shot, and then, Steve, you can chime in as well. But I think a couple of things, Bobby. Certainly, the dynamic of when the pandemic hit in

2020 certainly had a big impact on all of our businesses in that segment. So, we had significant volume impacts in Automotive. Aerospace held up for a little bit, but then went down in PHC as well.

So, the good news is, I think, that we see the outlook for volumes increasing across all three of those businesses and in Automotive, we can dig into that in more detail, if you like, but more a second half environment. So, we had – while they're not as big, Aerospace and Hydraulic Cylinders were a pretty decent-sized drag, right, on the EBIT margins there. And then as we got into the sort of back half of last year, we started to see some inflationary impact on raw materials and transportation costs in Automotive. But it wasn't as significant towards the end of last year, but it's been increasing as we go into this year. And we also, we mentioned, had a struggle with some operational difficulties in one of our North American operations and we're making sequential improvement in that.

But that has been pretty impactful as well on margins. And the team there has really stepped up and people from all around the world really have gone to help us turn that operation around and we're making good progress and we expect to see sequential improvement, particularly as we go into Q2 and the rest of the year there. So, all that being said, this has been impactful negative on our margins there. But I'm very optimistic and, I think, reasonably optimistic that we will return to the – closer to those historical margins that you quoted.

Bobby Griffin Q
Analyst, Raymond James & Associates, Inc.

Okay. Thank you. That's helpful. I guess two quick ones then. One, just inventories up, pretty high adverse sales, I think up 30% year-over-year of sales is up closer to 15%. Is that just the extra rod inventory and wire inventory that was built with the steel plant furnace changes you're doing or is there anything else there to unpack?

J. Mitchell Dolloff A
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

Yeah. Bobby, and Tyson chime in here. But I think it is that extra rod billet inventory that we have as safety stock there, which will work down pretty quickly...

Tyson Hagale A
Senior Vice President, President-Bedding Products, Leggett & Platt, Inc.

Second quarter.

J. Mitchell Dolloff A
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

...in the second quarter and then I think the impacts of inflation as well still hit us there.

Tyson Hagale A
Senior Vice President, President-Bedding Products, Leggett & Platt, Inc.

Yeah. That's right, Mitch. And I think the only other spots would be just where we've had some areas where we have really long supply chains and we've had some extra stock that we've been keeping in place just so we can ensure that we can comfortably support our customers. But we expect those will kind of work their way out through the course of the year.

J. Mitchell Dolloff A
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

Yeah. That's a really good point. I mean, I think we mentioned it in the opening remarks, but you and the team have taken a really balanced approach to say, hey, let's invest a little bit in labor, let's hold on to inventory and make sure we can service our customers. But overall, it's a – generally, inventory is in pretty good shape, right, from a US spring – perspective.

Tyson Hagale
Senior Vice President, President-Bedding Products, Leggett & Platt, Inc.

A

Yeah. Overall, I'd say we're in a pretty good place other than just we're making what we think are reasonable investments.

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

A

Yeah.

Bobby Griffin
Analyst, Raymond James & Associates, Inc.

Q

Okay.

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

A

That helped, Bobby?

Bobby Griffin
Analyst, Raymond James & Associates, Inc.

Q

Yeah, that's very helpful. And then lastly, Mitch, I mean, there was just a modest trim on the volume guidance. And you guys mentioned the quarter came in pretty in line with expectations. So, I just want to make sure I understand kind of what changed to the volume guidance. Is it just what you saw late in the quarter with some of the uncertainty or are you just factoring in that there should be a little bit more weakness going forward, given what's taking place in the world with new shutdowns and things like that? Just trying to understand, has it been what you've seen over March or April that surprised you or is it just expectations going forward?

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

A

I think it's both, probably, right.

Bobby Griffin
Analyst, Raymond James & Associates, Inc.

Q

Okay.

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

A

I mean, we saw lower demand starting to materialize, as Tyson commented, in Bedding overall. So, that was part of the driver there. And then, but then we've seen increased volumes in Work Furniture, optimistic about what we'll see in – as we talked about in Specialized throughout the year, particularly in the second half of the year there. So, I think it reflects the benefits of the diversity of our business, right. We saw some things go a little bit more negative and some things go a little bit more positive, which allowed us to hold the guidance overall, but make appropriate shifts.

Bobby Griffin
Analyst, Raymond James & Associates, Inc.

Q

Okay. I appreciate the details. Best of luck here.

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

A

Okay. Thanks, Bobby.

Operator: Thank you. We have next question from the line of Peter Keith with Piper Sandler. Please go ahead.

Peter Jacob Keith
Analyst, Piper Sandler & Co.

Q

Hi. Yeah. Thanks. Good morning, everyone. I hope you're doing well. Maybe just a follow up on that last part around Specialized. I was curious around the volume growth guidance that you're baking in on the Specialized segment for mid- to high-single-digit growth.

And presumably, that would bake in Automotive, getting quite a bit better since that's, by far, the largest business within Specialized. So, maybe just help frame that up a little bit more. It does seem like the demand backdrop for Automotive is falling off. I understand there's supply chain issues and restocking, but what's really embedded in there for Automotive as you look towards the back half of the year and what are the drivers to get it better?

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

A

Yeah, sure, Peter. Thanks. I don't see the part of the consumer demand falling off, I think inventories are at all-time lows, not only in the US, but around the world. So, I think there's still a big backlog of consumer demand. We've got aging vehicles, so it's going to take some time to work through that, which – and as well as restock inventory. So, I think that is a longer-term tailwind for the Automotive sector. So, I think that that outlook, we just have a different viewpoint on.

In terms of how we see the year playing out, really, I think that if we look at the major markets, vehicle production was down about 5% in the first quarter. Of course, we were just down 1%. It's forecasted to be about flat in Q2 and then significantly improved, about 20%, 21% in the third quarter and 6% or 7% in the fourth quarter. And that just kind of relates back to last year was stronger in the first half and then Q3 of last year was the low point versus some recovery in this point.

So, overall for the major markets, the full year is up around 4.8% in terms of production. So, that gets you to mid-single digits right there. Also benefit – in that, North America is up the most, about 13%; and Asia has been pretty strong. So we mentioned, Europe has been the most impacted with the Ukraine invasion, but our mix is the smallest in Europe about 17% and about 35% or so in North America and about a little less than 50% in Asia. So that favorable regional mix helps us and we also think we'll have some incremental awards that'll help us hopefully move beyond that mid-single-digits points there. And then we also talked about the volume gains, pretty significant in Aerospace and PHC. And so while they're smaller businesses – more hydraulic cylinders business, while they're smaller, that's helpful as well. So we feel like that mid to high single-digit range there is quite reasonable.

Peter Jacob Keith
Analyst, Piper Sandler & Co.
Q

Okay. That's a very helpful detail. Separately, it did note that the EBIT margin for the Furniture, Flooring, & Textile segment was up rather substantially by 230 basis points. Could you just walk us through the drivers to that? And is that type of improvement sustainable?

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.
A

Yeah. I mean, that's a great job by our team there, really glad to see that. But, Steve, do you want to jump in on that one?

Steven K. Henderson
Executive Vice President, President-Specialized Products and Furniture, Flooring & Textile Products, Leggett & Platt, Inc.
A

Yeah. Sure. Good morning, Peter. Yeah. Every business in this segment was extremely disciplined in their approach to understanding their costs and using pricing to offset inflation for not just raw materials, but labor and freight throughout the quarter and into this quarter. So that's the primary actions on top of the, as Mitch mentioned, the volume growth in Work Furniture offsetting some of the slowdowns in the other BUs. But it's really the pricing that [indiscernible] (00:39:11) to those two businesses.

Peter Jacob Keith
Analyst, Piper Sandler & Co.
Q

Okay. Great. Maybe I'll sneak in with just one last one. So, understand everything that's going on with the bedding market and the recent slowdown in demand. You're not the only firm that's expecting more stability in the back half. But I wanted to dig in more into the specialty foam because the volumes there were down 20% and it just doesn't feel like the market is nearly down that much. So, is there some share loss going on with specialty foam? What's really happening with that segment, particularly in light of recent anti-dumping duties that seems like they should be shifting production back to the US?

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.
A

Tyson, I'll let you take that one, I know you've been working on that.

Tyson Hagale
Senior Vice President, President-Bedding Products, Leggett & Platt, Inc.
A

Sure. Sure. Good morning, Peter. Yes. Understand the question, and we do feel like there are some additional headwinds in that part of our business. Just with the customer base that we serve there has been a bit more challenging of late. I've heard others talk about this and we agree the cost of acquisition where we typically service a lot of customers in the e-commerce channel has gone up and that seems to have been more challenged of late than even the more traditional channels. So, that's certainly been a factor.

Do feel like we're still working through some of the issues that we faced last year when we had shortages of chemicals and foam and had to, unfortunately, place our customers on allocations and so, still working our way through that part of it as well. Our team's been working really hard to pivot and diversify our customer base as well. As our chemicals have become more stable, we've also been returning to sell more products outside of Bedding into Furniture Products, also working with our customers on expanding their channel reach and some new products that help us there as well. So, doing what we can, but that is an area where we have faced some additional headwinds of late.

Peter Jacob Keith
Analyst, Piper Sandler & Co.

Q

Okay. Very helpful. Thanks a lot, guys, and good luck.

Tyson Hagale
Senior Vice President, President-Bedding Products, Leggett & Platt, Inc.

A

Thanks Peter.

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

A

Thank you, Peter.

Operator: Thank you. We have next question from the line of Susan Maklari with Goldman Sachs. Please go ahead.

Susan Maklari
Analyst, Goldman Sachs & Co. LLC

Q

Thank you. I just have a couple of follow ups for you. One, I guess, is across the call, you've definitely given some commentary on demand trends and what you're seeing across various end markets and channels in the business. But when you sort of take a step back and you think about the consumer overall, because I think that there is a lot of concern about their health and their ability to continue to spend at the level that we've seen more recently. What are you seeing in the business? How are you thinking about the overall health of the consumer?

And I guess then on the other side as well, it seems like from your commentary that the industrial side of your business has definitely strengthened and are seeing some healthier levels of demand. And so, I guess, one, is that right? And how are you thinking about those trends and maybe what is coming through there? And I guess also any commentary on Aerospace and any moves in the quarter in terms of those end markets?

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

A

Okay. Thanks, Susan. There's a lot to unpack. On the consumer trends, I mean, that's the big question out there, right, for everybody, and we watch it closely. It's particularly impactful to us in bedding and in home furniture and, as you said, some of those more consumer-facing businesses. But we are concerned about the impact of inflation. And as Tyson mentioned that it was holding pretty steady and then with the sort of shock in gas prices in the US and North America, I'd say, and then the conflict overall, the impact on Europe, right, that we did see some softening there.

But we'll see what's happened – what will happen, I think that if inflation starts to stabilize and maybe come down a little bit, people have still been spending. I mean, we saw it even in this last quarter with GDP down. When you go through the details, consumer spending was still pretty decent level. So, it is a big question. I think we are, I guess, optimistic that while it might soften a little bit, that it doesn't just fall apart.

So, I think that's reflected in our guidance. I think we have a pretty – a very realistic outlook for how we put those numbers together. I think you're also right that the industrial side of the business is picking up and it's great to see that.

We saw a very strong demand in Aerospace. We saw that improved – we've seen improved demand in Hydraulic Cylinders for quite some time and optimistic about what we see happening at Automotive and while I guess not directly industrial, even improvement in the contract side of our Work Furniture business. But Steve, do you want to add some more detail or color around Aerospace or Hydraulics Cylinders?

Steven K. Henderson
Executive Vice President, President-Specialized Products and Furniture, Flooring & Textile Products, Leggett & Platt, Inc.

A

[Technical Difficulty] (00:44:00) our customers are [Technical Difficulty] (00:44:02-00:44:10) Our assembly business is operating at historical levels and the [indiscernible] (00:44:15) business is recovering still lower than normal, but we're now having that manpower to fulfill that demand [Technical Difficulty] (00:44:22). There is a little uncertainty with the Ukraine invasion.

But that being said, the [indiscernible] (00:44:30), which is the industry experts [Technical Difficulty] (00:44:33) overall market increase of 22% this year and aircraft backlogs remain high. So, I think [Technical Difficulty] (00:44:42) work through the recovery, we're going to see that continued improvement there.

From a Hydraulics perspective, our OEMs, their forecasts are really strong for the rest of the year. But we're seeing short-term volatility to all the reasons we talked about [indiscernible] (00:45:00) some raw material availability, transportation and labor. But we did see production kick up pretty significantly in March, which is encouraging. We're not sure how sustainable that is in the face of the challenges, but the backlog has been above historical levels for 17 consecutive months and it really is [indiscernible] (00:45:23) at 16 months of backlog right now, an uptick of several quarters to work down minimally if they are able to maintain the March levels of production. So [indiscernible] (00:45:34) some stability for this year anyway.

Susan Maklari
Analyst, Goldman Sachs & Co. LLC

Q

Okay. That's very helpful. And I guess just following up on that a bit, when you look at the pricing power, I mean, you're continuing to see some really exceptional levels of pricing across the business and especially coming up against some really tough comps in there, which I think truly speaks to your ability to realize that and be able to offset the inflation in there. But as you look out, how do you think about the puts and takes of that? Meaning, is there any sort of kind of negative mix shift that you're seeing? Or how do you think about sustaining volume versus price as we do go forward and anything that could come through from that perspective?

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

A

Yeah. It's a great question. And I'd say a couple of things. And Tyson, I'll let you chime in on this. We talked about it the other day. But we're not seeing negative mix shift at this point. But there are opportunities, right, if increased inflation does start restricting consumer demand, then we can work with our customers to improve some of that. But I would say the baseline increases in raw materials, in labor costs, in transportation costs are so extreme and have been over the last couple of years that it's not a situation where you're fighting with your customer to say, well, you should absorb them because it's just too much. And so I think across – about all of the end markets that it's been passed through, like really I've never seen it before because it's big enough that it has to be. But Tyson, I'll let you add to that.

Tyson Hagale
Senior Vice President, President-Bedding Products, Leggett & Platt, Inc.
A

Yeah. No, Mitch, I totally agree. I mean, it's been a global event and at levels that can't be simply absorbed. And I think the industry all the way through the value chain has done a good job recognizing the magnitude of the impacts and passing it through. But it's definitely something that we're watching, we know our customers are watching it as well. And I do think that's part of our value proposition with our customers. We've always worked with them to understand, substitute product options and also value engineering options to help them work through other material efficiency options to help offset some of this as well. I mean, that's something we've done for a long time and are doing it right now, frankly. And that's something that we definitely have to bring to the table for our customers. It's part of the advantages that we have.

Susan Maklari
Analyst, Goldman Sachs & Co. LLC
Q

Okay. So that...

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.
A

Yeah. [indiscernible] (00:47:47).

Susan Maklari
Analyst, Goldman Sachs & Co. LLC
Q

Go ahead. I'm sorry.

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.
A

I'm sorry. I was just going to say it helps our customers and helps us as well. So, making sure volume is stable.

Susan Maklari
Analyst, Goldman Sachs & Co. LLC
Q

Yes. No. Absolutely. And I appreciate all that color. And so, I will – I'll end it there. That was very helpful, though.

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.
A

All right. Thank you, Susan.

Operator: Thank you. There are no further questions at this time. And I'd like to turn the floor back to Susan McCoy for closing comments. Over to you.

J. Mitchell Dolloff
President, Chief Executive Officer & Director, Leggett & Platt, Inc.

Susan, are you there?

Operator: Susan, over to you for closing comments.

Susan R. McCoy

Senior Vice President-Investor Relations, Leggett & Platt, Inc.

Sorry. I'm sorry. I did that again this quarter. I'm sorry. Thank you for joining us today. We'll speak to you again on August 2 after we report our second quarter results. If you have questions in the meantime, please contact us using the information in yesterday's press release. Thank you.

Operator: Thank you. Ladies and gentlemen, this concludes today's teleconference. You may disconnect your lines at this time. Thank you for your participation.