



**Fortune Brands Innovations, Inc.
Third Quarter 2025 Earnings Conference Call
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Presenters

Curt Worthington, Vice President of Finance & Investor Relations

Nick Fink, CEO

Jon Baksht, CFO

Q&A Participants

Susan Maklari - Goldman Sachs

Michael Rehaut - JPMorgan Chase & Co

Philip Ng - Jefferies LLC

Mike Dahl - RBC Capital Markets

John Lovallo - UBS Investment Bank

Trevor Allinson - Wolfe Research

Operator

Good afternoon, everyone. My name is Stacy, and I will be your conference operator, today. Welcome to the Fortune Brands Third Quarter 2025 Earnings Conference Call.

All lines are muted to prevent background noise. Following the speakers' remarks, we will open the floor for a Q&A session.

At this time, I'll turn the call over to Curt Worthington, VP of Finance and Investor Relations. Curt, please go ahead.

Curt Worthington

Good afternoon, everyone, and welcome to the Fortune Brands Innovations Third Quarter Earnings Call. Hopefully, everyone has had a chance to review the earnings release. The earnings release and the audio replay of this call can be found on the Investors section of our fb.in.com website.

I want to remind everyone that the forward-looking statements we make on the call today, either in our prepared remarks or in the associated question-and-answer session, are based on current expectations and market outlook and are subject to certain risks and uncertainties that

may cause actual results to differ, materially, from those currently anticipated. These risks are detailed in our various filings with the SEC.

The company does not undertake any obligation to update or revise any forward-looking statements, except as required by law. Any references to operating profit or margin, earnings per share or free cash flow on today's call will focus on our results on a before charges and gains basis, unless otherwise specified. Please visit our website for our reconciliations of these non-GAAP financial measures to the most directly comparable GAAP financial measures.

With me on the call today are Nick Fink, our Chief Executive Officer, and Jon Baksht, our Chief Financial Officer. Following our prepared remarks, we have allowed time to address some questions.

I will now turn the call over to Nick. Nick.

Nick Fink

Thanks, Curt, and good afternoon to everyone. Thank you for joining our call.

In the third quarter, Fortune Brands Innovations had solid sales performance and outperformed our end market, demonstrating the power of our brands and our people. Our sales in the third quarter were roughly flat versus the same quarter of 2024. And when excluding China, increased 1%.

From a point-of-sale perspective, excluding China, we estimate that we outperformed the market by almost 200 basis points, with a low single-digit point-of-sale growth.

While consumer sentiment and housing activity are still facing near-term pressures, our team is focused on execution and advanced several key strategic initiatives.

Our balance sheet remains very healthy as we continue to generate strong free cash flow and continue investing behind our core growth initiatives. We remain focused on our strategies while leveraging our Fortune Brands advantage capabilities to continue to position the company for sustained above-market growth. We believe we are well positioned to continue outperforming our end market for the remainder of 2025 and into 2026.

On today's call, I will start by sharing an update on our transformation and provide some examples of how it is advancing our strategy and delivering results. Next, I will provide a perspective on the macroeconomic environment and why I believe our portfolio balances stability with exceptional growth opportunities. I will then close with an overview of our performance before turning the call over to Jon for a detailed discussion of our financial results, updates to our guidance for the remainder of 2025 and some thoughts on our emerging expectations for 2026.

The third quarter marked a major milestone in our company's evolution. We welcomed more than 500 associates into our new campus headquarters in the Chicago land area and achieved our hiring commitments, two years earlier than planned. The quality of our new hires has been exceptional. They have joined numerous top-performing associates from within the organization who are either local or elected to relocate, creating a powerhouse team. This combination provides an optimal mix of continuity and new perspectives.

While our headquarters consolidation is first and foremost about accelerated growth, it has also allowed us to take a very critical look at our capabilities, talent and investments to drive increased efficiency across the organization.

Our state-of-the-art campus is perfectly suited for our business unit-led organizational design, which is supported by dedicated centers of excellence. Our footprint now mirrors our strategy, and we're already seeing increased collaboration and elevated execution, which is starting to show in our results.

As I've said previously, this was the third of three phases of our transformation into a tightly aligned operating company. With most of this transition successfully behind us, I'm excited to see how we continue to accelerate performance in 2026, and beyond.

Throughout this transformation, we've maintained a consistent overarching strategy. Our brand strength, focus on innovation and expertise in channel management create a compelling value proposition and drives our performance. Our execution of this strategy leverages Fortune Brands Advantage capabilities, which are category management, business simplification, global supply chain excellence and digital transformation.

These strengths enable us to rapidly adapt to shifting markets, increase market share and deliver innovation at scale. Our alignment into an execution-focused operating company is allowing us to better leverage strengths across our organization with tangible results, this quarter.

Using advanced analytics, data science and deep insights into customers and consumers, we are able to implement precise strategies for pricing, promotions and product assortment. This precision allows us to maintain a careful balance between margin protection, price stability and demand responsiveness and facilitates sustainable share growth over the long term, even amidst a dynamic external environment.

We continue to expect to fully offset the anticipated in-year dollar impact of tariffs in 2025 and the anticipated annualized dollar impact in 2026 through a combination of supply chain actions, cost-out opportunities, and strategic pricing actions.

Fortune Brands has consistently acted as the price leader in our categories and our high integrity, transparent and collaborative approach to tariff pricing was consistent with that

history of leadership. As a result, our tariff-related pricing was relatively modest, and absent any new significant tariffs, is now largely in the market.

While some of our competitors are still taking significant additional tariff pricing, our work for 2025 tariff pricing is essentially complete and has been for some time. That positions us, well, to focus on execution, strengthen channel relationships and preserve pricing integrity, while allowing us to capture additional share. We intend to opportunistically look for areas to now promote and drive volume.

Now turning to the external environment. The macro environment remains uneven, with consumer sentiment cautious and housing activity showing mixed signals. However, our demand profile is stable, and we see green shoots heading into 2026. As we enter the final quarter of 2025, the U.S. housing market continues to show signs of stabilization, following a period of elevated mortgage rates and constrained affordability.

While overall home sales remain subdued, recent rate cuts by the Federal Reserve have helped ease borrowing costs with a 30-year fixed mortgage rate dipping to its lowest level in a year and almost a full point below where they were at the start of 2025.

This has sparked renewed buyer interest and a surge of refinancing activity, suggesting that pent-up demand may begin to unlock, as affordability improves.

Home inventory levels are also rising, particularly in the South and West, giving buyers more options and helping shift the market toward a more balanced state.

Prior business, which is primarily focused on repair and remodel, the mid- to longer-term outlook remains encouraging. In the near term, R&R is below trend, even when normalizing for the post-COVID period. However, we believe R&R is poised to rebound in the not-too-distant future, driven by aging housing stock and deferred maintenance projects, as well as a consumer base which is increasingly interested in renovating their homes.

For example, a recent survey indicated that 84% of homeowners plan to renovate a part of their home in the next 12 months. Record levels of tappable homeowner equity, together with lower rates, means that homeowners are in a strong position to finance improvements through equity extraction tools like HELOCs and cash out refinancing.

Recent data shows that homeowners are utilizing home equity lending methods at the highest rates since 2022, with momentum building. Across our channels and segments, we compete in smaller ticket categories where consumers look to trusted brands and innovation to deliver value. Even in the trade down environment, our brands were made the preferred choice by pros and consumers because they combine quality, style, innovation and reliability at accessible price points.

Our single-family new construction, which comprises roughly one quarter of our total sales has faced headwinds from elevated rates and cautious builder sentiment, it remains a long-term driver of growth, supported by a shortage of existing homes. As interest rates continue to trend downward and consumer confidence stabilizes, we anticipate a recovery in single-family activity, which we expect will provide additional growth, across our portfolio.

Our products are well positioned to benefit from the torque of new construction growth with manageable downside risk. Our products are not affected by homebuilders reducing square footage for affordability, since efficient design changes do not significantly change the number of faucets, valves or entry doors within a home. In fact, many of our products can contribute to improved housing affordability because they are easy to install, durable, and can even help save money through reduced insurance premiums and utility costs.

It is also important to note that the vast majority of our products are installed later in the construction process, which results in lower variability since completions serve as a moderating factor compared to the more volatile starts.

Finally, our relationships with builders positions us as the incumbent brand preferred by both professionals and homeowners when these homes eventually engage in repair and remodel activity.

Overall, we believe our balanced portfolio provides stability while also offering attractive growth potential, which comes with new construction. With our advantaged footprint and brand strength, we are confident in our ability to continue outperforming our end market and are poised for accelerated growth.

Turning to our third quarter performance, sales were roughly flat at \$1.1 billion, and excluding the impact of China, were up 1%. Our margins were 17.9% and earnings per share were \$1.09.

Turning to our segment highlights, our Water segment delivered another quarter of market outperformance. Sales were \$619 million, down 3% versus third quarter of 2024. Excluding China, net sales were roughly flat. Importantly, our point-of-sale results, excluding China, were up low single digits versus a market which we estimate was slightly down.

In Moen, we executed the strategic and targeted promotional activity that we called out during our second quarter call, driving momentum and strong sell-through with key partners. We increased our share with all three of our largest retail partners during the quarter, and Moen continues to be recognized as the most trusted brand of faucets.

Our brand strength with both consumers and the pro is increasingly evident. Our innovative products continue to win external accolades including Moen's recent inclusion on Time Magazine's Best Inventions of 2025 list.

In wholesale, demand remained resilient. Importantly, our relationships with key builders remain very strong, as we not only resigned a number of our key national builders, but also converted others to the Moen brand, resulting in further share gains. We are well-positioned with builders due to Moen's exceptionally strong value proposition and our superior service capabilities and we expect to continue to take additional share in this category.

The House of Rohl portfolio saw significant sales growth over the third quarter of 2024, and delivered low double-digit point-of-sale growth, significantly outpacing the broader market. Our luxury consumer remains strong and continues to prioritize craftsmanship and design. Our brands are strategically positioned to capitalize on sustained demand, and the work we have done to build our luxury brands portfolio is yielding positive results. We expect this to continue to serve as a growth platform through the rest of 2025, and beyond.

Turning to e-commerce, this channel has rebounded since our reset earlier in the year. We are seeing the benefits of our updated go-to-market approach, coupled with the refreshed talent and expertise in our team. We generated sequential improvement within e-commerce sales in the third quarter. There is still room for further improvement, and we see upside momentum heading into fourth quarter of 2025 and into 2026.

In Digital Water, Flow continues to exhibit very strong growth. We recently launched the initial trial of the leak protection service, our new recurring revenue model subscription service. While it is too early to share any results, interest in a Flow subscription is very strong, and we expect this to be a meaningful unlock in both the consumer and insurance channels.

We believe Connected Water will serve as a growth engine for years to come, given its differentiated value proposition and potential to significantly decrease one of the largest drivers around housing affordability, insurance costs.

In Outdoors, we continue to execute, well, in the softer market environment. Sales were \$345 million, roughly flat versus third quarter of 2024. We estimate that our segment point-of-sale outperformed our end market by over 300 basis points, with market outperformance across our brands.

In LARSON, the rollout of our retail aisle reset helped drive double-digit sales growth in the third quarter. Our new approach to innovating and marketing storm doors drove a strong consumer response including point of sale, which was up high single digits versus a roughly flat market.

This initiative also received external recognition. Earlier this month, Lowe's named LARSON its 2025 Vendor Partner of the Year for the Lowe's Millwork division. This is a significant honor and a proof point of the underlying investment thesis in LARSON and the ability of Fortune Brands to drive value through its disciplined and returns-focused capital allocation strategy.

Therma-Tru strongly outperformed its category with point-of-sale share gains in both wholesale and retail. Although net sales decreased in the third quarter, this was primarily due to the absence of the usual fall inventory build. However, strong customer orders in early October suggest that this decline has not continued into the fourth quarter.

In Q3, a significant milestone was reached in the American fiberglass door coalitions case against Chinese fiberglass door panel imports. The court has put in place preliminary countervailing subsidy duties ranging from 50% to 900% on Chinese fiberglass door panel imports. The U.S. government continues its investigation and a final decision is expected in Q1 of 2026. We expect to see the benefit of this government action, in addition to tariffs as Chinese inventory in the market is consumed.

Fiberon performed well in the third quarter. In September, we recorded the highest monthly sellout for the year. Fiberon saw sales growth in the third quarter versus last year in both retail and wholesale, with strong point-of-sale outperformance in wholesale.

Our Outdoor brands benefit from their vertically integrated U.S. manufacturing presence, giving them an advantage over import reliant competitors. We expect to see the benefits of our North American footprint to become more apparent in 2026.

Turning now to Security. Our Security segment also made progress in the third quarter. Sales were \$186 million, up 5%, building off of many of the initiatives we have highlighted last quarter with further momentum expected in the coming quarters.

The Master Lock and SentrySafe brand campaigns continue to build upon our industry-leading awareness and drive consumer engagement. During the quarter, we secured several new retail placements in a variety of outlets and across multiple price points, as competitive products are proving to be inferior alternatives to our iconic and trusted brands. We expect to see the benefit of these retail wins in the fourth quarter and into 2026.

Finally, the recent Prime Day exceeded our expectations, and we have gained share in the growing e-commerce channel, throughout 2025. As we look toward the end of the year and 2026, we are confident that we will see growth due to our focus on strategic execution.

Digital security solutions are also gaining traction, and we see a robust pipeline of opportunities for both residential and commercial applications. Recently, our Yale Assure Lock 2 received accolades, including being named Best Smart Lock by CNET and the Spruce. The launch of the Yale Smart Lock with Matter, designed for Google Home, is also delivering encouraging early results.

Turning now to our full digital portfolio. Our digital portfolio continues to scale, and we're making strong progress. We now have over 5 million registered users across our digital platforms with strong momentum in new device activations.

For Digital, overall, we have full conviction in the strength of our product portfolio and its ability to deliver differentiated, sustained growth over the long term.

With respect to Flow, we continue to add and expand partnerships with insurance companies and the data shared regarding the product's effectiveness for both homeowners and insurers continues to affirm its significant impact.

For Yale, we won several new retail placements and have a significant number of partnerships, which we are starting to scale more broadly.

Across our Digital businesses, we are increasingly leveraging our well-established advantaged channel relationships with builders, retailers and wholesalers to drive new opportunities. The fundamentals of our Digital strategy are sound, and we remain confident in the potential of this growth platform. We are on track to approach \$300 million in annualized sales by the end of 2025 with continued growth into 2026.

To recap, the third quarter was another strong demonstration of Fortune Brands' ability to execute with discipline, respond with agility and deliver above-market performance. Our teams are advancing our transformation, strengthening our brands and investing in platforms that create new avenues for growth.

Looking forward to the fourth quarter of 2025, we expect to deliver year-over-year sales growth and market outperformance and expect to see the continued benefits of the initiatives that we have detailed in the call. Throughout the recent periods of external uncertainty and market disruption, we have remained focused on what we can control, driving our most strategic investments, continuing to support our leading brands and strategically reshaping our business to be leaner, stronger and more agile.

These moments of challenge have been opportunities for us to optimize our structure, sharpen our priorities and position ourselves for accelerated growth when conditions improve. Today, we stand not only resilient but designed for performance and built for the future.

I will now turn the call over to Jon.

Jon Baksht

Thank you, Nick. Before I begin, I want to thank those who participated in our recent investor perception study. Your insights will inform our Investor Relations practices, and we are actively working to implement improvements.

As part of this effort, we are reviewing how we consistently present period comparisons, certain performance indicators and growth narrative, particularly in areas like digital innovation and other key portions of our portfolio. We'll look to incorporate these enhancements, beginning next quarter.

As a reminder, my comments will focus on results before charges and gains to best reflect ongoing business performance. Additionally, comparisons will be made against the same period last year, unless otherwise noted.

In the third quarter, we again delivered solid results against a soft market backdrop. We delivered sales of \$1.1 billion, roughly flat year-over-year. Our results reflect lower volumes compared to last year, which were partially offset by strategic pricing actions implemented earlier this year.

Sales were up 1%, excluding the impact of the China business.

Consolidated operating income was \$206 million, down 5% compared to last year, largely due to lower volumes and higher cost of goods, partially offset by pricing, lower incentive compensation and disciplined cost management.

Operating margin declined 80 basis points to 17.9% due to lower volumes and product mix in Outdoors and Security. EPS was \$1.09.

Turning to our segments, beginning with Water, sales were \$619 million, down 3%, reflecting lower volume, partially offset by price. Excluding China, our sales were roughly flat on a year-over-year basis, reflecting low single-digit POS growth offset by lower inventory build, compared to prior year and modest inventory destocking in Canada.

Water's operating income was \$151 million, down \$5 million compared to last year. Operating margin was 24.4%, down 20 basis points compared to last year, reflecting our efforts to strategically balance price realizations and operating costs. We continue to expect full year water margins to be in the range of 23% to 24%.

Turning to Outdoors, sales were \$345 million, roughly flat compared to last year, with pricing offsetting lower volumes. Sales benefited from the momentum from the LARSON perfect aisle reset and continued share gains of Fiberon. Point-of-sale increased low single digits versus a market that was down low single digits. This is partially offset by lower seasonal channel inventory builds in Therma-Tru in the third quarter, as wholesale customers reduced orders in response to weaker external data points.

We are encouraged that orders have increased entering the fourth quarter and are trending higher, year-over-year.

Outdoors operating income was \$53 million, down \$8 million compared to last year, with operating margin of 15.5%, a decrease of 250 basis points from the third quarter of 2024. These results reflect the impact of lower volumes, higher material costs and product mix, partially

offset by price. We expect to maintain margins at similar levels in the fourth quarter and for the full year, we expect segment margins in the 13% to 14% range.

In Security, sales were \$186 million, up 5%, with price offsetting lower volumes with strong growth in e-commerce and the commercial business. Our Master It brand campaign for Master Lock is resonating, driving a double-digit increase in brand engagement and contributing to improved sell-through.

Security operating income was \$33 million, down \$1 million year-over-year. Operating margin was 17.8%, down 150 basis points versus third quarter 2024, largely due to product mix, as well as increased investments in product development during the quarter, consistent with our strategy to invest in future growth throughout the cycle. For the full year, we expect margins in the 15.5% to 16.5% range.

Turning to the balance sheet. We are managing our capital structure with the objective of balancing our cost of capital, returns and overall flexibility. We ended the quarter with cash of \$224 million. Net debt stood at \$2.4 billion with net debt-to-EBITDA leverage of 2.7x, consistent with our deleveraging objective.

We remain on track to end the year with net debt to EBITDA at the upper end of our previous guidance range of 2.2x to 2.5x.

Free cash flow in the quarter was \$177 million. We now expect full year free cash flow of \$400 million to \$420 million, reflecting reduced operating income, higher working capital levels and higher cash restructuring charges, compared to last year.

Additionally, our headquarters transition continues to progress ahead of our original timetable. As a result, during the quarter, we updated the range for total restructuring costs related to the headquarter transition to \$100 million to \$120 million. The increase relative to our previous range reflects the faster completion of the transition with higher estimates for severance, accelerated depreciation, lease termination costs and other refinements.

We remain opportunistic with our capital allocation, balancing shareholder returns with investments to drive growth and M&A opportunities that align with our strategy.

Before turning to our outlook, I'll provide an update on our tariff exposure. As Nick mentioned, we are still on track to fully offset the anticipated impact of tariffs, both in 2025 and on an annualized basis in 2026. Implemented changes in tariff rates and rules since our last call have only had a de minimis impact to our unmitigated tariff exposure, but the overall tariff environment has contributed to a more cautious consumer and margin pressures.

As a reminder, we have worked to get our spend from China down significantly and expect to be around 10% of cost of goods sold by the end of the year. Our predominantly North American supply chain remains a differentiated competitive advantage.

Turning now to our outlook, we are pleased with our year-to-date performance amidst the dynamic macro environment. As today's press release details, we are narrowing our EPS guidance and anticipate finishing the year near the low end of our prior range, reflecting the impact of mix and lower volumes within an uncertain end market. The full details of our updated guidance can be found in our press release.

As we look beyond 2025, we are actively planning for a variety of scenarios. While it is impossible to predict the exact timing of a demand inflection, we continue to believe it is a matter of when, not if, and when the demand inflects. We believe we are uniquely positioned for above-market growth.

While we will not be providing guidance assumptions for 2026 at this point, we are able to share some initial thoughts. Our base planning assumptions center around a flat market, overall. Importantly, we believe we are well positioned for our sales to outperform this market estimate, based on the meaningful opportunities for which we have line of sight.

Through our transformation, we are continuing to identify efficiencies and continuous improvement opportunities throughout our business and remain confident in our ability to drive value, even in a dynamic market environment.

In summary, our third quarter results, once again, demonstrate the resilience of Fortune Brands' portfolio, the strength of our brands and the effectiveness of our advantaged capabilities. We are laser-focused on executing our strategy while investing in the innovations and capabilities that will fuel our long-term growth.

I'm confident in our ability to continue executing at a high level, as we close out 2025 and look ahead to 2026.

I will now pass the call back to Curt to open the call for questions.

Curt Worthington

Thanks, Jon. That concludes our prepared remarks. We will now begin taking a limited number of questions. Since there may be a number of you who would like to ask a question, I will ask that you limit your initial questions to two and then reenter the queue to ask additional questions. I will now turn the call back over to the operator to begin the question-and-answer session. Operator, can you open the line for questions. Thank you.

Operator

If you would like to ask a question, please press "*", followed by "1" on your telephone keypad. A confirmation tone will indicate that your question has been added to the queue. To withdraw your question, press "*", followed by "2". If you are using a speaker phone, please

pick up the handset, before pressing the star keys. Once again, that's "*", followed by "1" to ask a question.

First question comes from Susan Maklari with Goldman Sachs. Please go ahead.

Susan Maklari

Thank you and good afternoon, everyone. My first question is on the pricing strategy. Nick, thank you for all the comments on that and the approach that you've taken there, this year. I guess given that, can you talk a bit about how the outcomes have come together? Have they been in line with what you have expected as you approach the pricing? And how you're thinking about this going forward.

Nick Fink

Sure, Sue, I'd be happy to. Look, as we said, I think on our prior calls and you've tracked us for a long time, as you know, from prior inflationary periods, we maintain a very disciplined approach to pricing. And so, as we think about it, our goal is, as category leader, to lead where we have to lead but do it in a clear, transparent and incremental way. And if we feel like if we do it and we do it well and we do it early, then we can do it in small increments.

And if you recall, 2021 through that inflationary period, we were also taking kind of single, mid-single-digit pricing because we were doing it early and we were covering our cost.

Now I will say, before I touch further on pricing, I mean, we do a lot before we get to pricing. We work our supply chain really hard. We've pursued a lot of cost-out initiatives. And then what we're not able to mitigate through that, we turn to pricing. And in the case of 2025 with the tariffs, we did that very early on. And we said consistently, since that time, that between all of those actions, we will cover off on tax. We've covered off on tariffs, and we're do.

I've read reports that we're "behind" in our second round. There is no second round. We did it early, as I said, in the beginning of the year, we got it done. It's behind us.

And really, what we're doing now is we're focusing our enhanced data capabilities and actually looking at places that we can lean into the market and drive volume; where are those opportunities to promote, understand the elasticities. If we have further CI, we're going to hunt for more of those opportunities, and we think that's what is driving a lot of the share gain that we're seeing. And so, I'd say we've been consistent on it through this tariff period, but we've been consistent on it through '21, through the inflationary period in '17.

And what we find is, sometimes, it takes a while for others to follow. And that may mean that, that causes a headwind for us for a quarter or two, and that's fine. We're playing a long game, and we're playing to gain share over the long run, and we'll do it in the highest integrity way for ourselves and our customers. And I think that's exactly what's playing out now.

Susan Maklari

Okay, that's great color. And maybe building on that, one of the things that Fortune has historically done really well is outperforming the market and gaining share in periods of weakness. And it certainly sounds like from your comments, that is coming through again. But I think something that differentiates you today is this investment that you do have in data, right, a lot more information and nuances of understanding things. How is that helping you to better target those share gains and perhaps even better sustain and further grow the business, even as things normalize and we eventually return to market growth.

Nick Fink

Yes, look, it's a great question. It's a very exciting part of our strategy. I'll say, as you know, we've been on this broader digital journey now for a little more than half a decade. And I'd say the greatest thing about that, whether it's product, whether it is digital initiatives that are customer-facing or internally facing, the whole team is digitally fluent at this point.

I'm not going to say we're digital natives, but we can get around the table and we can discuss digital innovations and understand them. And that's allowed us to move very quickly, particularly as some of these AI tools have become available.

And so, when I think specific to your question around something like pricing, I mean, I remember several years ago, when we first invested to build our pricing analytics, and I think they were best-in-class at the time. Today, I say that is pretty antiquated compared to what we have today, which is, A, much more precise and, B, much faster moving, where we can really get insights on a SKU-by-SKU level. And some of the new leadership that we have here with our headquarters transformation has brought in just world-class talent. And so, we're getting sharper and foster all of the time.

That's on the pricing side. We're also able to do things like customer and consumer insights literally in hours, whereas it may have taken us weeks. So, once you understand exactly where your customer is, where your consumer is, what their shopping behaviors are, what their switching behaviors are and how to target them, it makes us a much more fierce machine.

Now for all of that said, I think we're just at the early innings of doing this. We've got some great people and some great capabilities in place. We're seeing some unbelievable talent as we continue to hire up as part of our transition and transformation to the new headquarters, but I think it's early innings for what you'll see us do with these capabilities.

Susan Maklari

Yeah, okay, that's great. Thank you for the color and good luck with the quarter.

Nick Fink

Thank you.

Operator

The next question, Michael Rehaut with JPMorgan. Please proceed.

Michael Rehaut

Thanks. Hi, good afternoon. Thanks for taking my questions. First, I wanted to hit, and I'm sorry if I missed this in the prepared remarks, but just to get a dial in a little bit more in terms of what was driving the 100 basis point decline in segment margin guidance for Outdoor and Security, particularly, as we're kind of sitting here at the end of the third quarter, kind of curious what's changed in the last 90 days to drive that type of decline. And if the third quarter margins in either segments, in part, reflected maybe some of that change in outlook or performance.

Nick Fink

Sure, Mike. I'm happy to try to take it at the highest level, and then Jon can round it out if you'd like some more detail. In Outdoors, a very simple story. By the way, we saw great performance out of that segment, particularly at the point-of-sale level. What we did not see was the usual seasonal inventory build that you see at this time of year in preparation for the next building season. I've seen this happen once before where we don't see that build, and that tends to be pretty margin-rich product, relative to the rest of the portfolio.

So in Outdoors, it was pretty much just a mix inside of that inventory build, not particularly concerned about it because that inventory will have to be built to serve that market, at some point. And I mentioned, it will be at some point next year.

And in Security, I'd say it's a variation on that theme. We saw a strong commercial performance, but we did see some backing off from our B2B business. And yet, we maintained our R&D investment at a higher level than prior, and we maintained marketing investment at a higher level than prior, particularly with our new Master campaign, which is doing really, really well, and notwithstanding a bit of a mix shift there, we did not want to pull back on those investments.

Jon, if you want to add anything?,

Jon Baksht

Maybe just to maybe put some numbers around it for you on the inventory piece for Outdoors, Mike. If you look at last year, the seasonal inventory builds, typically, we do see low double-digit increases in that channel inventory in Q3. This year, it actually went the other way, and we saw low double-digit declines.

And so, to Nick's point, that's something that we'll have to reverse, and so it is a bit of a Q3 dynamic. As we go into Q4, not sure if that's going to reverse then or into next year. But like we mentioned in the prepared remarks, October has seen some signs, early signs of that reversal. And so, we're encouraged that, that is on the comm.

Michael Rehaut

Okay. I appreciate that. Maybe I'll follow up a little later on that, as well. Secondly, I wanted to take a step back or shift the question to Digital. Nick, I believe you said that you're on track to hit the \$300 million annualized rate -- run rate by the end of this year. I wanted to get a, sense kind of two parts here. One, tried to dimensionalize those sales between plumbing and security, number one. And secondly, I know you've thrown out, I think, I want to say by 2030, but I could be wrong there, the \$1 billion sales goal.

Really would love though to try and understand how to think about the growth in the business. I'm not asking necessarily for guidance but just directionally or degree of magnitude, how to think about growth in 2026, '27 off of -- I guess, if you did \$300 million, maybe that would be growth technically, but how to think about that annualized run rate, let's say, going forward.

Nick Fink

All right. I'll just start by kind of giving couple of things to wrap your head around and then say some stuff about some of what you're looking for. So on the first part, yes, we're approaching that \$300 million annualized, which is what we were hoping to see at this point. And also, I think on the prior call, we said expect it to end this year around \$250 million. We're actually tracking a bit ahead of that. So really satisfied with the way that business continues to develop.

Very, very strong growth on the Flow side, continue to be extremely excited about the opportunities there. And we just very, very recently launched our subscription service, which is the leak protection service, which we think takes a huge barrier to growth away because even though the value prop of Flow is very clear to us, very clear to insurers, there's still a price barrier for a lot of people.

And the research that we said though, says they're absolutely happy to pay a monthly subscription, particularly if their insurance savings is even greater than that subscription, right? It's just a win-win-win, a win for us, a win for the insurer, a win for the consumer. And so very excited that, that has now launched, and we'll be back to you as we start to see the data of how that's performing.

On the security side, it's -- we're seeing some nice things. I referenced some of the Yale progress in my prepared remarks, but I think there's more opportunity to come as we cycle in some of the new products, some of which we've developed with Google and some of the big partnerships that we have signed up, which will roll into 2026.

One further thing I'll say, and then Jon may give some more color. I think those of you who participated in our recent feedback survey, and it was very helpful. And we understand that people want more dimension around this. And I think, over time, we've tried to share anything that we could that is verifiable, repeatable and auditable, like those are our standards for sharing numbers. I understand there's desire for more.

And so, we're going to come back at the beginning part of the year with, I think, just a clear set of metrics that we're going to be reporting to regularly for the digital business, just if you bear with us, hopefully. And we're taking feedback as to what people are looking for and to the extent we can share, we will.

Jon Baksht

Yeah, absolutely, Mike. And just to build on the disclosure for next year, it's -- when you start looking at 2030 metrics, it's always harder to build the road map to those. And as we build out the framework for reporting, we do want to provide something that is more tangible in the near term that you can look at.

And what I would say to your question around the split between security and outdoors, we don't disclose that at the moment, just given the relative size in our overall portfolio, they're both rapidly growing. And so that piece -- and I'd also give you just some broad guidance that neither of them is outsized in the portfolio. There's a good balance between both security and water within that connected build. But we'll provide a broader framework going into next quarter that will be a bit easier to follow, going forward.

Nick Fink

So just to sum it up, because that was the last part of your question, trending ahead of the \$250 million that we gave last quarter, very happy about that. Approaching the \$300 million annualized, very happy about that and absolutely convicted about the \$1 billion by 2030.

Michael Rehaut

Great, thanks so much.

Operator

The next question, Philip Ng with Jefferies. Please go ahead.

Philip Ng

Hey, guys. Yeah, great to hear about how you're -- you've done. You've pushed through your pricing raise for plumbing on the Water side, right? It sounds like your peers, Nick, are playing a little catch-up. Does that put you in a position to play offense? Any color on how you're performing by end markets, retail channels? Any early read on like placement by any of these markets that we should think about for 2026?

Nick Fink

Sure. Let me take the second part first, and then we'll come back to playing offense because it is helpful for just crystal clear. We're very happy with the Water results. I'll just start there. If I look at the opportunities, build there, we're gaining share, very pleased. Retail gained share across all three majors; we're very pleased.

As we said on the last call, we saw opportunity to improve our performance in e-commerce. We have a new team in place. We're executing with, I'd say, significantly upgraded capabilities, uncovering a lot of opportunities. Happy with the progress, but room to improve. Expect to see that improvement, as we come through this year and into next year.

As I think about then offense, the answer is, absolutely. As we work hard, very hard, in fact, to continue to mitigate the impact of tariffs, we're still working with supply chain, we're still working on cost efficiencies. We're going to look to redeploy that where we can to meet the consumer where they are and promote as we can. And so, it's not signaling anything dramatic. But with a lot of this effort behind us, we see opportunity to then really sharpen the pencil.

Jon Baksht

And one piece that Nick didn't mention in there, but mentioned in the prepared remarks is House of Rohl. And that continues to see really outsized growth really across the distribution. What we're seeing is a lot of strength with the luxury consumer. And within our -- you name the metric between volume, price, we're seeing some very good indicators in the luxury segment.

Nick Fink

Yeah, absolutely.

Jon Baksht

Yeah, I mean, the margin has been stellar.

Philip Ng

Then Jon, you gave us a little hint that 2026 in terms of the end markets, but you're expecting to outgrow. One, it'd be great if you could quantify how much but more importantly, can you flag some of the areas where you think you've had some wins that give you confidence that perhaps you could grow a little faster than the market? And then any directional help how we should think about margins as well?

Jon Baksht

Yeah, it's still premature to start quantifying things, Phil. We're just working through the 2026 plan, right now. We do have some visibility into the market environment, which is where I guided that. This year, which has been a slightly down environment, we are looking next year to be largely flat. And so, while that's the market backdrop hasn't seen a significant turn, we are seeing a bit of some constructiveness in the market to keep it flat.

We do feel comfortable that we're going to outperform the market. And you can just look at this quarter's results. I think through our largest business unit, Nick just went through a lot of the wins that we're seeing in the marketplace in Q3 and what we're seeing in the early parts of Q4, and we expect those to continue into next year.

And if you go across each of our business units, there's individual pieces that provide that confidence. Starting with Water, I think Nick just covered off on those. If you go through Outdoors, we've talked about LARSON perfect aisle. Really, we've seen some good turnarounds at Fiberon in terms of some of our productivity and efficiency there. Therma-Tru, we talked about some of the lack of seasonal inventory builds, which that will start to rebound.

In addition to that, we've also mentioned some of the antidumping tariffs that have been coming into the market in that particular segment, which we also think will be a nice tailwind for us.

In Security, we've continued to invest going into next year. So we've got some good momentum around our Master It campaign that we feel will continue. The new rollout of our connected products and the Yale Google Smart locks, I think, are going to be a nice tailwind for us, as well. And then you just layer on the connected business and watch the growth we're seeing in Flow and our Connected products. So, a lot to be excited about going into next year to drive that outperformance.

Philip Ng

Super. Really appreciate the color, guys.

Nick Fink

Thank you.

Operator

The next question, Mike Dahl with RBC Capital Markets. Please go ahead.

Mike Dahl

Hey, thanks for taking my questions. I just want to start with kind of a clarifying question around the tariff dynamic. Obviously, still some moving pieces since you last gave your guidance between kind of copper and maybe some refinement around 232's and now the most recent news about reduced China exposure.

And Nick, I wasn't sure if your comment referred to the 2025 impacts being de minimis, but maybe can you just clarify that, talk about kind of on an annualized basis as all tariffs, as currently announced, and maybe inclusive of this reduction in China tariffs, what that gross impact is for you.

Nick Fink

Yeah, I'll just make a quick comment and turn it to Jon. But I'd just say on the de minimis, we're not processing in that the 10% yet. That's very late-breaking, and we want to do some work on that, so we're talking about all the other changes as we work through it. And then there's some sector-specific challenges, too, that we see. You've referenced some of them that we're going to have to be laser-focused on. I think with respect to the late-breaking news on the 10%,

firstly, we want to see it actually get inked and then we will do our work around that to see where there's opportunity.

Jon, do you want to give some more color.

Jon Baksht

Yeah, happy to give some color. So I think on the last call, I gave some dimensions around the tariff impact, \$80 million in 2025 and \$260 million on an annualized basis in 2026. So since that, since the call, we've seen the reciprocal tariffs come down quite a bit and really across many of the jurisdictions. And so currently, and frankly, even with some preliminary views of the 10% reduction on China that was announced this morning, we see that the \$80 million for this year is likely baked in. But on an annualized basis for next year, we're more in the low \$200 million range, more in the low \$200 million area, I would say.

So the tariff impact has come down. And as you mentioned copper, copper was introduced since the last earnings call but inclusive of my comments on the low 200s, that includes copper, which really has been de minimis for us. I think our estimate for the overall copper impact across our businesses is around \$3 million. So not much of an impact at all.

And again, we are focused on mitigating these tariffs through a variety of actions. So supply chain actions, which we continue.

We are estimating that our -- that around 10% of our COGS will be China-based by year-end. So we've been taking a lot of actions there, cost-out opportunities that both Nick and I have mentioned throughout the call and then the strategic pricing actions, which is the third item. But really, it's a combination of those three that have helped us work that down, and we feel we've done a lot of work on these numbers, and we feel very comfortable on where we stand.

Mike Dahl

Yes, that's very helpful and good to hear. And if I just shift gears to a little more near term, you talked about a lot of the dynamics already, but I wanted to drill down on Water margins for 4Q, just given the commentary around now looking to pick your points on promotions and where to lean in on volume. Your guide still implies kind of a wide range of outcomes for the fourth quarter. So can you help us kind of ballpark what that fourth quarter margin impact? And also maybe, specifically, like within that range of kind of the Water guide, how you're leaning on top line as well when you think about 4Q, specifically?

Jon Baksht

Sure. I'm happy to start off. From a margin decline standpoint, we did guide to the full year for Water. Our margin guidance from quarter-to-quarter has not changed. So we maintain our 23% to 24% operating margin in that business unit. And so if you play that out, that still implies close to 23% or around 23% margin for that business unit in the fourth quarter, which would still be a nice increase, or at least a modest increase from Q4 of last year.

And I would tell you that just from a sequential basis, if you think about the margin decline, it's really just a matter of mix and spend. And we've mentioned some of the spend that we've been doing from promotional activity. I think that's probably one area that might change. And then the mix within our products and our channels, we're seeing a little bit of movement there, as well.

Mike Dahl

Yes, thank you.

Operator

The next question, John Lovallo with UBS. Please go ahead.

John Lovallo

Hey, guys, thank you for taking my questions, as well. Maybe just to follow up on Mike's question there. I mean I think you gave -- just gave the Water margin directionally, and I think you gave the Outdoor being similar in the fourth quarter to the third quarter. But I guess the question is, we're about 10 months into the year, and it feels like the overall ranges here are still pretty wide. Curious what could kind of swing things directionally here within the next couple of months in such a wide range? And maybe if you could just give us a little bit more color by segment on where you're kind of leaning as we stand today?

Nick Fink

Yeah, John, this is Nick. I'll start with just a couple of conceptual things, and Jon will fill in some color. Just firstly, I would say the way we think about margins, we play it for the year, not for the quarter, right? We're trying to run the business over the longer term. And so, we're not going to move around investments quarter-to-quarter to just try to hit a margin number. We're building this thing for the longer run.

And so that's, B, I'd say some of the variability has come from some of the inventory and channel movements that we've seen this year, whereas Jon referenced, like we didn't see a seasonal inventory build in a high mix part of the business that will come down the road. But that does have some impact on margin.

And then just the third comment on margins, generally, is I'd say we'd look to the full year guidance on it. And then with respect to the tariff pricing, I think it's important to note, like we're -- our goal is to cover off tariffs dollar for dollar, and then we will work back any margin that we need to work back over time, leveraging our CI initiatives and our supply chain initiatives.

Jon Baksht

Yeah, and I think just to quantify it a little bit, if you look at our full year guide, which Q4 is always an interesting one because we do a full year guide, and it's really just one quarter, so

you can back into our Q4 margin guidance. And if you look at what that is for both Outdoors -- we covered Water, so my comment is on Outdoor & Security. You can really -- you can see that our Q4 margin implied in each of those guides is higher than the full year guidance so we are increasing our margin in both Outdoors & Security as we go into the back half of the year.

We talked about a lot of the dynamics in Outdoors in terms of the channel inventory. And I would say that if there's another factor kind of weighing on Outdoors, there is a mix element to it, as we look at our product mix. It weighed on us a bit in Q3, and that trend is -- it looks like it's going to be something that we face in Q4, as well.

And then in Security, I would say probably similar commentary. I think there is a mix element to it in terms of the timing of our promotional spend and when we're going to see some of that sales pull through. And one of the other elements on security that maybe we haven't touched on, on the call is there is a bit of, as we change some of the -- start selling through some of our new technology and some of the new hardware, the mix of some of the old hardware that we're also selling is at a lower price point is probably playing a little bit of a part in Q4, as well.

John Lovallo

Okay. Got you. And then, Nick, maybe just from a higher-level strategic angle here. I mean, there's obviously been a number of pretty meaningful changes at Fortune recently with leadership, corporate headquarters, etc. And it seems like a lot of this is behind you at this point, maybe you can kind of refocus on the core business.

So my question is, how comfortable are you with the current categories and brands? Are there any that maybe don't quite fit in quite as well as you thought, prior? Or are there any areas that you would look to add to? I mean, how are you kind of looking at the portfolio overall?

Nick Fink

Yeah, I'll just start with where you started, which was referencing that transformation. And I would say, as I said earlier, we kind of feel like we're at the end of Phase 3 of 3 of really coming down to a very tightly run operating company. And that first big portfolio move in '22 with cabinets and then moved to an operating company model, business unit led, refined that. I think some lessons learned, frankly, of things we could have done better.

So made some structural and management changes at the start of this year, kind of I call that Phase 3 of 3 and went to a footprint that matched our strategy with the headquarters move, which we've now moved over 500 people into, and we're off and running. And so, we're actually really excited to have that behind us and really just go into '26 focused on execution and some of the incredible talent that we have here.

Just a couple of other things I'll say. In addition to the talent story, this is all about driving growth, right? It's all about being tighter, leaner, leaner together and driving growth. It is also

unlocking some efficiencies, right? When you just have less duplication and you're together and you can move faster, you're going to be more efficient, and we're seeing that.

And then just a final thought, as I said before, is in what is still a challenging economic backdrop, because we've gone through this, we're still in the rehiring phase, and we have our hand firmly on that throttle, and we will throttle it as appropriate to not over hire in what is still a challenging economy. And so, that's given us a lot of flexibility with our SG&A, short of having to go what we're seeing others do in the marketplace and actually let people go. And so, that's a really good backdrop. So good question around the portfolio.

I mean, we are always looking at both our own portfolio and evaluating what are the most productive and fit to strategy parts. We will continue to do that. That's part of our duty to our shareholders as well as looking outside, but we will remain extremely disciplined, which is to say we look for good businesses, we look for businesses where we can add value, and we will only do it at prices that we believe are compelling where we can drive return.

And so there's some interesting things out there that could help us move the strategy along even faster, but it would have to meet that criteria.

John Lovallo

Okay, thank you, guys.

Nick Fink

Sure.

Operator

The next question, Trevor Allinson with Wolfe Research. Please go ahead.

Trevor Allinson

Hi, good evening. Thank you for taking my questions. I wanted to follow up on your comments about a flat market in 2026. I appreciate it's early, but we're seeing the homebuilders continue to slow starts pretty aggressively here, which will impact you guys on a lag. So, considering that's well less than half of your business, is the assumption that you all see repair and remodel growth next year and that will offset a declining new res market or how do you think about growth or declines in each of those markets getting you to a flat overall market?

Nick Fink

Yeah, I'll just give some high-level comments and Jon can jump in. First, just as a reminder for the builder side of the business, which is about a quarter of our business, we are much more tied to the midpoint between starts and completions, and they aren't typically one for one. What you'll see it starts to move up and down. The completions are much, much more steady, and that's much closer to the number that we see come through our business because, again, the builders can throttle the starts number up and down.

And then, we are seeing recovery in the R&R line. I think -- I'd like it to be a whole lot stronger, but I was just looking at some data points across retail and e-commerce. And actually, the market has been flat for us on a dollar basis for 10 straight weeks, which I hate to say that it's exciting, but relative to the last two, three years, that's actually pretty decent.

And so, you are seeing some firming. And then, of course, we're seeing things like the home equity extraction activity, applications for HELOCs, things like that, like I think up 80%, I read in the last report, so some green shoots there. And then we do have our growth initiatives in things like digital and luxury, which will provide us a tailwind to overdrive versus that market.

Jon Baksht

Yeah, and I think just to add on that, if you look at what we've seen in some of those markets kind of year-to-date and how that might play into next year, in Repair and Remodel, this is our biggest segment. If you look at the beginning of the year, we were looking at that being a bit -- that was still a bit down and a little bit of a drag, although we have seen that turn in the back half of the year, and we expect some of that to continue to next year.

So as I look at a flat overall market, we're looking at probably low single-digit increase in Repair and Remodel, with still some challenges in single-family new construction, that probably down low single digits. So those will offset each other, and then that will play out through our portfolio.

Nick Fink

So I'd just add, this isn't our '26 guide. We're trying to give our perspective to be helpful. If things improve, we'll invest accordingly. But if things deteriorate, as I said earlier, we've got our hand very firmly on that SG&A throttle, particularly with some roles yet to fill. And so, we're going to navigate this very, very tightly.

Trevor Allinson

Right. Yeah, I appreciate that, and the color is extremely helpful. And then one of your competitors in Water is out with a large, announced price increase early next year. I just want to make sure I'm hearing your commentary correctly regarding price. Is it your expectation at this time that offsets to tariffs, moving forward, are going to be through avenues other than pricing, and it's not currently your expectation to push pricing in early 2026 to cover tariffs specifically? And then if you could, can you just tell us what Water pricing was up on a year-over-year basis in 3Q? Thanks.

Nick Fink

Yeah, I'll start. I don't know if we've broken that out, but I'll start on just how we're thinking about it. So as we said, our pricing on a dollar-for-dollar, not a margin basis, a dollar-for-dollar basis, we believe we've covered off on the tariffs as we know them today. That said, as I said earlier, like the philosophy of this company as a category leader is to be extremely disciplined in pricing, so we will take pricing. We will take it on a regular basis, and we'll take it in, hopefully,

small increments. So that's our strategy. And that's what we did here, we had mid-single-digit pricing across the portfolio to cover off on tariffs.

If you go back to '21, where we saw massive inflation, you had pretty modest pricing. Why? Because we took it early. We did it consistently.

And as long as we continue to flex that muscle and we do it highly strategically focused where the market can accept that pricing and less so where the market cannot, leveraging some of these digital capabilities we built, then we should be in a very good position. And we really believe in doing that, and we really believe in maintaining pricing integrity across our channels, best for all of our customers.

And so that's what I would expect to see from us as we move from here into '26. But what I don't believe you will see at this point, absent any new tariff news to the negative is any type of catch-up pricing. As I said, I want to be crystal clear about that. There is no second round for us. We're done.

Trevor Allinson

Thank you for all the color. Good luck, moving forward.

Nick Fink

Thank you.

Jon Baksht

Thank you.

Operator

Thank you for joining today's conference call. You may now disconnect.